HAWAII EMPLOYER-UNION
HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

Annual Financial Report

June 30, 2010

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To the Board of Directors of
the Hawaii Employer-Union Health Benefits Trust Fund
of the State of Hawaii and
Ms. Marion Higa, State Auditor
State of Hawaii, Office of the Auditor
Honolulu, HI

Independent Auditor's Report

We have audited the accompanying statements of net assets (deficit) for the enterprise fund and fiduciary assets and liabilities for the agency fund of the Hawaii Employee-Union Health Benefits Trust Fund of the State of Hawaii (Trust Fund) as of June 30, 2010, and the related statements of revenues, expenses and changes in net deficit, and cash flows for the enterprise fund for the year then ended. These financial statements are the responsibility of the Trust Fund's management. Our responsibility is to express opinions 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust Fund'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 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 opinions.

As discussed in Note 1, the financial statements of the Trust Fund are intended to present the financial position, and the changes in financial position and cash flows, of only that portion of the activities of the State of Hawaii this is attributable to the transactions of the Trust Fund. They do not purport to, and do not present fairly the financial position of the State of Hawaii as of June 30, 2010, and the changes in its financial position and its cash flows for the year 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 respective financial position of the enterprise fund and agency fund of the Trust Fund as of June 30, 2010, and the respective changes in financial position and, where applicable, cash flows 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 our report dated August 15, 2011, on our consideration of the Trust Fund'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 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.

Management's discussion and analysis listed in the table of contents is not a required part of the basic financial statements 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 Trust Fund has not presented revenue and claims development information that accounting principles generally accepted in the United States of America require to supplement, although not be part of, the basic financial statements.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Trust Fund's basic financial statements. The schedule of administrative operating expenses (Schedule) is presented for purposes of additional analysis and is not a required part of the basic financial statements. The Schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Macias Gini & O'Connell LLP

Newport Beach, California

August 15, 2011

This section of the Hawaii Employer-Union Health Benefits Trust Fund of the State of Hawaii (Trust Fund) financial report presents the reader with an introduction and overview of the Trust Fund's financial performance for the years ended June 30, 2010. This discussion has been prepared by management and should be read in connection with the financial statements and the notes thereto, which follow this section.

Chapter 87A of the Hawaii Revised Statutes (HRS) established the Trust Fund. The Trust Fund is the state agency that provides eligible State of Hawaii (State) and County (Honolulu, Hawaii, Maui and Kauai) employees and retirees and their eligible dependents with health and life insurance benefits at a cost affordable to both the public employers and participants beginning July 1, 2003. HRS Chapter 87 that established the Hawaii Public Employees Health Fund (Health Fund) was repealed and the net assets of the Health Fund were transferred to the Trust Fund.

During 2007, the Trust Fund adopted Governmental Accounting Standards Board Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other than Pensions* (GASB 43). GASB 43 establishes accounting and financial reporting standards for plans that provide other postemployment benefits (OPEB) other than pensions. GASB 43 requires a statement of plan net assets and a statement of changes in plan net assets for defined benefit OPEB plans that are administered as trusts or equivalent arrangements. However, if an OPEB plan is not administered as a trust or equivalent arrangement it is required to be reported as an agency fund.

Further, the reporting of active employee and retiree (including their respective beneficiaries) healthcare benefits provided through the same plan should separate the two benefits for accounting purposes between active employee and retiree healthcare benefits. Accordingly, the Trust Fund reports the retiree healthcare benefits as OPEB in conformity with GASB 43 and the active employee healthcare benefits as risk financing in conformity with adopted Governmental Accounting Standards Board Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues* (GASB 10) as amended.

In August 2006, the Trust Fund issued a Request for Proposals seeking proposals to provide benefit plans effective July 1, 2007. The evaluation committee recommended and the Board of Trustees approved the award of contracts for twelve benefit plans for the period July 1, 2007 through June 30, 2009.

Beginning July 1, 2007 the Trust Fund began offering self-funded medical and prescription drug plans. Under self-funded arrangements, the Trust Fund contracts with plan administrators for provider networks, claims processing, cost containment and other services. Instead of premiums, the Trust Fund pays administrative fees to the contractor and reimburses the contractor only for claims paid.

The Board of Trustees approved exercising its option to extend the contract for two years (July 1, 2009 through June 30, 2011) for Hawaii Dental Service, Hawaii Medical Service Association, Health Management Associates, Kaiser Foundation Health Plan, Inc., Royal State National Insurance Company, Vision Service Plan and for two one year extensions (July 1, 2009, through June 30, 2010, and July 1, 2010, through June 30, 2011) for informedRx and Standard Life Insurance.

Effective February 1, 2010, the Trust Fund Board of Trustees approved a new 80/20 PPO plan administered by Hawaii Medical Service Association (HMSA). The 90/10 PPO plan was administered by Health Management Associates (HMA).

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements of the Trust Fund include the following statements:

Enterprise Fund - *Active Employee Healthcare Benefits*

Statement of net assets (deficit) - This statement summarizes the assets and liabilities and presents an overall picture of the financial position.

Statement of revenue, expenses and changes in net deficit – This statement summarizes the financial results of the operations for the year.

Statement of cash flows – This statement identifies the sources and uses of cash.

Agency Fund - *Retiree Healthcare Benefits*

Statement of fiduciary assets and liabilities - This statement summarizes the financial position of the OPEB plan assets and liabilities reported as an agency fund.

FINANCIAL HIGHLIGHTS

The Trust Fund collected in the aggregate $513,232,601 and $160,081,601 in employer and employee contributions for the health benefit plans and Medicare reimbursements, respectively, and paid carriers in the aggregate $157,684,549 and $433,056,598 and retirees $44,830,546 in premiums, self-insured claims and Medicare reimbursements, respectively, for the year ended June 30, 2010. The monthly premiums for the Trust Fund's benefit plans include administrative fees that are intended to cover the Trust Fund's administrative expenses. The aggregated administrative fees collected from the employers totaled approximately $5,117,032 for the year ended June 30, 2010. The Trust Fund reported $1,268,524 for carrier retrospective premiums payable as of June 30, 2010.

The administrative expenses budgeted for the Trust Fund totaled approximately $5,212,288 for the year ended June 30, 2010. Actual administrative operating expenses for the enterprise fund totaled $4,334,911 for the year ended June 30, 2010. The expenses included $1,668,784 for personnel services; $1,787,862 for consultant services; $179,828 for equipment; $314,994 for lease rent; and $383,443, for other expenses such as open enrollment, office supplies, telephone, travel, repairs and maintenance, copier rental and postage for the year ended June 30, 2010.

For the year ended June 30, 2010, the presentation of the operations of the self-insured plans for active employees reported in the enterprise fund was changed to show the aggregate amount of premium revenues recognized as operating revenues and related benefit claims expense incurred as operating expenses. This change was a result of the financial reporting criteria of GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues* (GASB 10), where the risk of loss for these self-insured plans transfers from the employers to the Trust Fund, thus the activity should be reported in aggregate in the statement of revenues, expenses and changes in net deficit. The 2009 amounts in the Financial Analysis section below have been restated to reflect this change in order to be comparable to the 2010 amounts.

FINANCIAL ANALYSIS

Enterprise Fund

A summary of the Trust Fund's net assets (deficit) for active employees is shown below as of June 30, 2010 and 2009:

	2010	2009*	Change	% Change
Assets				
Current assets	$ 36,830,892	$ 32,496,347	$ 4,334,545	13.3%
Capital assets	8,658,429	6,554,713	2,103,716	32.1%
Total assets	45,489,321	39,051,060	6,438,261	16.5%
Liabilities				
Current liabilities	49,734,089	56,296,172	(6,562,083)	-11.7%
Long-term liabilities	680,580	424,620	255,960	60.3%
Total liabilities	50,414,669	56,720,792	(6,306,123)	-11.1%
Net assets (deficit)				
Invested in capital assets	8,658,429	6,554,713	2,103,716	32.1%
Unrestricted	(13,583,777)	(24,224,445)	10,640,668	-43.9%
Total net deficit	$ (4,925,348)	$ (17,669,732)	$ 12,744,384	72.1%

* 2009 balances were restated to reflect amounts reclassified from the agency fund to the enterprise fund to better account for and report administrative costs to administer the Trust Fund. Balances affected include capital assets, current assets and current liabilities. See Note 12 to the financial statements for further details.

The enterprise fund's total assets increased by approximately $6.4 million or 16.5% during the fiscal year ended June 30, 2010. The increase is primarily attributable to the following: 1) an increase to active employee rates effective July 1, 2009, caused an increase of approximately $4.2 million to the premiums receivable from State of Hawaii and Counties, 2) an increase of approximately $2.3 million in deposits to HMA due to the increase in enrollment count for the 90/10 PPO plan effective February 1, 2010, 3) an increase of approximately $3.0 million in the capital assets due to the implementation of the new Benefits Administration System effective September 2009.

The enterprise fund's total liabilities decreased by approximately $6.3 million or 11.1% during the fiscal year ended June 30, 2010. The decrease is primarily attributable to the decrease of approximately $7.7 million in benefit claims liability payable to the self-funded carriers. There was also an increase in Trust Fund's OPEB liability.

There was approximately $12.7 million or 72.1% reduction of the Total Net Deficit for the year ended June 30, 2010. This is primarily attributable to the $14.6 million decrease in claims expense which caused a net gain in the self-funded plans.

A summary of changes in net deficit for the years ended June 30, 2010 and 2009 for active employees follows:

	2010	2009*	Change	% Change
Revenues				
Operating revenues	$ 258,717,861	$ 225,420,482	$ 33,297,379	14.8%
Nonoperating revenues	4,348,544	15,063,335	(10,714,791)	-71.1%
Total revenues	263,066,405	240,483,817	22,582,588	9.4%
Expenses				
Operating expenses	250,322,021	272,534,878	(22,212,857)	-8.2%
Total expenses	250,322,021	272,534,878	(22,212,857)	-8.2%
Increase (decrease) in net assets	12,744,384	(32,051,061)	44,795,445	139.8%
Net deficit at beginning of year, as restated	(17,669,732)	14,381,329	(32,051,061)	-222.9%
Total net deficit at end of year	$ (4,925,348)	$ (17,669,732)	$ 12,744,384	72.1%

* 2009 balances were restated to reclassify revenues related to self-insured plans as operating revenues and related claims expense as operating expenses. In addition, amounts previously reported as transfers are now classified as nonoperating revenues. Furthermore, amounts were reclassified from the agency fund to the enterprise fund to better account for and report administrative costs to administer the Trust Fund. Balances affected by the reclassification of agency fund activity include operating revenues and operating expenses.

The enterprise fund's total revenues increased by approximately $22.6 million or 9.4% for fiscal year ended June 30, 2010. The enterprise fund's operating revenues increased due to the increase in active employee rates effective July 1, 2009. The non operating revenues decreased due to $12.6 million decrease of subsidy from the agency fund.

The enterprise fund's operating expenses decreased by approximately $22.2 million or 8.2% for fiscal year ended June 30, 2010. There was approximately $900,000 increase in informedRx prescription drug rebate, $14.6 million decrease in claims expenses and $3.3 million decrease in incurred but not reported claims.

The enterprise fund's total net deficit changed by approximately $12.7 million or 72.1% for fiscal year ended June 30, 2010. This increase is attributable to the increase of active employee rates effective July 1, 2009, and the addition of the 80/20 PPO plan effective February 1, 2010.

Agency Fund

A summary of the Trust Fund's plan assets and liabilities for retirees is shown below as of June 30, 2010 and 2009:

	2010	2009*	Change	% Change
Assets:				
Cash and cash equivalents	$ 49,889,100	$ 32,159,322	$ 17,729,778	55.1%
Cash and cash equivalents - pre-funding deposits	135,182,090	93,707,587	41,474,503	44.3%
Receivables	31,098,553	27,041,670	4,056,883	15.0%
Deposits	10,248,076	10,092,000	156,076	1.5%
Total assets	$ 226,417,819	$ 163,000,579	$ 63,417,240	38.9%
Liabilities:				
Premiums payables	$ 5,716,500	$ 4,688,210	$ 1,028,290	21.9%
Benefit claims payable	12,867,761	14,318,267	(1,450,506)	-10.1%
Amounts held on behalf of employers for benefits	206,816,699	142,948,269	63,868,430	44.7%
Other	1,016,859	1,045,833	(28,974)	-2.8%
Total liabilities	$ 226,417,819	$ 163,000,579	$ 63,417,240	38.9%

* 2009 balances were restated to reflect amounts reclassified from the agency fund to the enterprise fund to better account for and report administrative costs to administer the Trust Fund. The agency fund no longer reports prepaid expenses, capital assets, vouchers and contracts payable, accrued wages and employee benefits, and compensated absences. See Note 12 for further details.

The agency fund's cash and cash equivalents increase of approximately $17.7 million was mainly attributable to the decrease of approximately $11.4 million in claims expenses during the year and a $1.2 million write-up of investments held in the State investment pool. The agency fund's cash and cash equivalents – pre funding deposits increase of approximately $41.5 million was attributable to the collection of pre-funding deposits for OPEB by various employers. The agency fund's receivables account increase of $4.1 million was attributable to the increase in retiree rates effective July 1, 2009 and January 1, 2010.

The agency fund's premiums payable increase of approximately $1.0 million was due to the increase in retiree rates. The agency fund's benefit claims payable decrease of approximately $1.4 million was attributable to lower claims expenses for fiscal year ended June 30, 2010. The amounts held on behalf of employees for benefits increase of approximately $63.9 million was attributable to the following: 1) an increase in OPEB pre-funding deposits by various employers, 2) write-up of investments held in State investment pool, 3) increase in net gain from the self-funded plans due to a decrease in benefit claims expenses and increase in premium revenue.

CAPITAL ASSETS

The aggregated net asset value of capital assets was $8,658,429 at June 30, 2010. The aggregated depreciation expense totaled $914,118 for the year ended June 30, 2010. In August 2007, the Trust Fund issued a Request for Proposal seeking proposals to furnish a benefits administration system implementation and maintenance services. The evaluation committee recommended and the Board of Trustees approved the award of a contract to provide, implement and maintain a Benefits Administration

System for the Trust Fund. The new Benefits Administration System was implemented in September 2009.

ECONOMIC FACTORS AFFECTING NEXT YEAR

Effective January 1, 2011, the Hawaii State Teacher's Association (HSTA) voluntary employees beneficiary association (VEBA) health benefit plan was terminated and all employees receive benefits through the Trust Fund. Approximately, 12,500 HSTA VEBA active employees and 2,500 retirees were transferred to the Trust Fund. In December 2010, Judge Sakamoto ruled that HSTA VEBA members (actives and retirees) were entitled to the same standard of coverage in benefits when they were transitioned to the Trust Fund on January 1, 2011.

In April 2011, the Trust Fund issued Request for Proposals seeking proposals to provide health and life benefit plans effective January 1, 2012. The evaluation committee recommended and in June 2011 and July 2011, the Board of Trustees approved the award of contracts for health and life benefit plans.

REQUEST FOR INFORMATION

This financial report is designed to provide the Board of Directors, State Auditor, and our membership, with a general overview of the Trust Fund's finances and to account for the money it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Hawaii Employer-Union Health Benefits Trust Fund
P.O. Box 2121
Honolulu Hawaii 96805-2121

Respectfully Submitted,

Barbara Coriell
Administrator

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

ENTERPRISE FUND
Statement of Net Assets (Deficit)
June 30, 2010

Assets		
Current Assets		
Receivables		
Premiums receivable from State of Hawaii and counties	$	23,024,861
Other receivables held by insurance companies (Note 5)		31,696
Rebates receivable (Note 5)		1,755,967
Accrued interest receivable		328,172
Prepaid expenses		181,516
Deposits (Note 6)		11,508,680
Total current assets		36,830,892
Capital assets, net of accumulated depreciation of $4,980,259 (Note 4)		8,658,429
Total assets		45,489,321
Liabilities		
Current Liabilities		
Vouchers and contracts payable		108,345
Accrued wages and employee benefits payable		109,786
Due to State of Hawaii		196,075
Due to employees		669,224
Retrospective premiums payable (Note 5)		254,142
Premiums payable (Note 5)		10,026,690
Benefit claims payable (Note 6)		38,334,060
Compensated absences, current portion		35,767
Total current liabilities		49,734,089
Noncurrent Liabilities		
Compensated absences (Note 2)		136,890
Other postemployment benefits (Note 8B)		543,690
Total liabilities		50,414,669
Net Assets (Deficit)		
Invested in capital assets		8,658,429
Unrestricted		(13,583,777)
Total net deficit	$	(4,925,348)

See accompanying notes to financial statements.

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

ENTERPRISE FUND
Statement of Revenues, Expenses, and Changes in Net Deficit
Year ended June 30, 2010

Operating revenues:		
Premium revenue-self-insurance	$	253,295,079
Administrative fee (Note 2)		3,019,049
Administrative fee-Agency Fund (Note 2)		2,097,983
Increase in premium reserves - fully insured risk sharing plans		305,750
Total operating revenues		258,717,861
Operating expenses:		
Claims expense-self-insurance (Note 6)		248,281,987
Change in incurred but not reported (IBNR) claims		(3,310,000)
Gain/loss on carrier payment methodology (Note 2)		101,005
Depreciation (Note 4)		914,118
Administrative operating expenses		4,334,911
Total operating expenses		250,322,021
Operating income		8,395,840
Nonoperating revenues (expenses):		
Interest income and other, net of fair value write up of investments held in State pool of $1,806,133		2,150,063
Subsidy from Agency Fund (Note 7)		2,198,481
Total nonoperating revenues (expenses), net		4,348,544
INCREASE IN NET ASSETS		12,744,384
Total net deficit at beginning of year, as restated (Note 12)		(17,669,732)
Total net deficit at end of year	$	(4,925,348)

See accompanying notes to financial statements.

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

ENTERPRISE FUND
Statement of Cash Flows
Year ended June 30, 2010

Cash flows from operating activities:	
Cash paid to vendors	$ (3,043,867)
Cash paid to employees	(1,510,134)
Cash received from State of Hawaii, counties and individuals for premiums and benefit payments	253,145,274
Cash paid for premiums and benefit payments	(252,157,355)
Rebates received related to prescription drug plan	1,234,302
Reserves returned by insurance carriers	854,021
Net cash used in operating activities	(1,477,759)
Cash flows from capital and related financing activities:	
Purchases of furniture, equipment and software development	(3,017,834)
Net cash used in capital and related financing activities	(3,017,834)
Cash flows from non-capital and related financing activities:	
Subsidy from Agency Fund	2,198,481
Net cash provided by non-capital and related financing activities	2,198,481
Cash flows from investing activities:	
Interest received	2,297,112
Net cash provided by investing activities	2,297,112
Net change in cash and cash equivalents	-
Cash and cash equivalents at beginning of year	-
Cash and cash equivalents at end of year	$ -

Reconciliation of operating income to net cash (used) by operating activities:	
Operating income	$ 8,395,840
Adjustments to reconcile operating income to net cash (used) by operating activities:	
Depreciation	914,118
Increase in premiums receivable from State of Hawaii and counties	(4,221,661)
Decrease in premium reserves held by insurance companies	854,021
Decrease in rebates receivable	1,234,302
Increase in prepaid expenses	(147,576)
Increase in deposits	(2,200,680)
Decrease in vouchers and contracts payable	(230,164)
Increase in accrued wages and employee benefits payable	(25,663)
Increase in amounts due to State of Hawaii	187,896
Increase in amounts due to employees	661,858
Decrease in retrospective premiums payable to carriers	(1,589,172)
Increase in premiums payable to carriers	2,164,162
Decrease in benefits claims payable	(7,659,353)
Increase in compensated absences	184,313
Total adjustments	(9,873,599)
Net cash used in operating activities	$ (1,477,759)

See accompanying notes to financial statements.

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

AGENCY FUND

Statement of Fiduciary Assets and Liabilities
June 30, 2010

Assets		
Cash and cash equivalents (Note 3)	$	49,889,100
Cash and cash equivalents - pre-funding deposits (Note 3)		135,182,090
Receivables		
Medicare reimbursements from individuals, net of allowance of $403,332		173,878
Premium receivable from State of Hawaii and counties		27,283,772
Other receivables held by insurance companies (Note 5)		24,584
Rebates receivable (Note 5)		3,385,529
Accrued interest receivable		230,790
Total receivables		31,098,553
Deposits (Note 6)		10,248,076
Total assets	$	226,417,819
Liabilities		
Due to State of Hawaii	$	62
Due to retirees		2,415
Retrospective premiums payable (Note 5)		1,014,382
Premiums payable (Note 5)		5,716,500
Benefit claims payable (Note 6)		12,867,761
Amounts held on behalf of employers for benefits		206,816,699
Total liabilities	$	226,417,819

See accompanying notes to financial statements.

(1) FINANCIAL REPORTING ENTITY

Chapter 87A of the Hawaii Revised Statutes (HRS) established the Hawaii Employer-Union Health Benefits Trust Fund (Trust Fund). The Trust Fund was established to design, provide and administer health and other benefit plans for State of Hawaii and County (Honolulu, Hawaii, Maui and Kauai) employees, retirees and their dependents beginning July 1, 2003. HRS Chapter 87 that established the Hawaii Public Employees Health Fund (Health Fund) was repealed and the net assets of the Health Fund were transferred to the Trust Fund.

The Trust Fund is administratively attached to the Department of Budget and Finance in the executive branch of the State of Hawaii (State). The Trust Fund's basic financial statements reflect only its portion of the fund type categories. The State Comptroller maintains the central accounts for all State funds and publishes annual financial statements for the State, which includes the Trust Fund's financial activities.

The Trust Fund is administered by a Board of Trustees (Board) composed of ten trustees appointed by the Governor of the State of Hawaii. The Board is responsible for determining the nature and scope of benefit plans offered by the Trust Fund, negotiating and entering into contracts with insurance carriers, establishing eligibility and management policies for the Trust Fund, and overseeing all Trust Fund activities. The Board relies on professional services provided by a salaried Administrator, the State Attorney General and a benefit plan consultant.

The Trust Fund currently provides medical, prescription drug, dental, vision, chiropractic, dual-coverage medical and prescription and group life insurance benefits. The medical plans include a statewide service benefit plan and a federally-qualified HMO plan. Other benefit plans are offered on a statewide basis.

The employers' share of benefit plan contributions for collectively bargained employees are negotiated by the State and Counties with the exclusive representative of each employee bargaining unit. Employer contributions for all other employees not covered by collective bargaining contracts and for retirees are prescribed by the HRS. Any remaining premium balance is paid by employees through payroll deductions or Premium Conversion Plan reductions.

State and county contributions also include the employees' share made through payroll deductions, contributions for retired employees, and Medicare reimbursements made by the Trust Fund to eligible retired employees and their spouses for Medicare Part B insurance premiums withheld from their social security benefits.

The Trust Fund provided insurance coverage to approximately the following individuals as of June 30, 2010:

	2010
Active employees	53,900
Retirees	39,285
Spouses	36,244
Domestic partners	1,059
Dependents under the age of 19	33,809
Dependents between the ages of 19-23 who are full-time students	6,296
Disabled dependents	432
Total	171,025

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Proprietary Fund (Enterprise Fund) - The accounting for the active employee healthcare benefits are reported as an enterprise fund. An enterprise fund is used to account for the acquisition, operation and maintenance of government facilities and services that are entirely or predominantly supported by user charges. The enterprise fund operations are reported using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of the timing of cash flows.

The enterprise fund statements apply all effective pronouncements of the Governmental Accounting Standards Board (GASB). In addition, these statements apply all Accounting Research Bulletins (ARBs) of the Committee on Accounting Procedures, Accounting Principles Board Opinions (APBO) and Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989, except those that conflict with GASB pronouncements. The Trust Fund has elected not to apply the FASB pronouncements on accounting and financial reporting that were issued after November 30, 1989.

The enterprise fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services or goods in connection with the enterprise fund's ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. The principal operating revenues of the Trust Fund are premium contributions and administrative fees. Interest income from investments is reported as nonoperating income.

Fiduciary Fund (Agency Fund) - The Trust Fund reports assets and liabilities in an agency fund resulting from the collection of contributions from employers and retirees and payments of postemployment health benefits for retirees and their beneficiaries.

The Trust Fund follows GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other than Pensions* (GASB 43). GASB 43 establishes accounting and financial reporting standards for plans that provide other postemployment benefits (OPEB) other than pensions. GASB 43 requires organizations to report a statement of fiduciary assets and liabilities – agency fund for multiple-employer OPEB plans that are not administered as trusts or equivalent arrangements. For fiscal year 2010, the Trust Fund does not meet the criteria of a trust or equivalent arrangement, thus assets and liabilities for the postemployment health benefits are reported as an agency fund.

The agency fund is reported using the same basis of accounting as the enterprise fund. The agency fund is reported using the accrual basis of accounting. The agency fund reports no plan net assets and the assets accumulated in excess of liabilities is reported as a liability for amounts held on behalf of employers for postemployment health benefits.

Financial Statement Presentation **-** The reporting of active and postemployment (including their respective beneficiaries) healthcare benefits provided through the same plan should separate the two benefits for accounting purposes between active and postemployment healthcare benefits. Accordingly, the Trust Fund reports the postemployment healthcare benefits in conformity with GASB 43 and the active employee healthcare benefits as risk financing in conformity with GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues* (GASB 10), as amended. The Trust Fund administers postemployment healthcare benefits under an agent multiple-employer defined benefit plan as defined by GASB 43.

In 2010, the accounting for the active employee healthcare benefits are reported under the statement of net assets (deficit) – enterprise fund, statement of revenue, expenses and changes in net deficit – enterprise fund and statement of cash flows – enterprise fund. The accounting for the postemployment healthcare benefits are reported in the statements of fiduciary assets and liabilities – agency fund. For financial reporting purposes, certain assets, liabilities, revenues and inflows and expenses and outflows have been allocated for the separate accounting of active employees and postemployment healthcare benefits.

Capital Assets

The Trust Fund's capital assets consist of furniture, equipment and software with estimated useful lives greater than one year and with an acquisition cost greater than $5,000. Purchased capital assets are valued at cost. Donated capital assets are recorded at their fair value at the date of donation. Depreciation expense is determined using the straight-line method over the assets' useful life of seven years.

Cash and Cash Equivalents

Cash and cash equivalents represent amounts held in and by the State Treasury. The Trust Fund invests funds in the State Treasury cash and investment pool (State Pool) as well as directs the State Treasurer to invest in specific investments outside of the State Pool. Investments are reported in the accompanying statement of net assets (deficit) and statement of fiduciary assets and liabilities at fair value. Changes in fair value that occur during a fiscal year are recognized as interest income in the statement of revenues, expenses and changes in net deficit and as a change in amounts held on behalf of employers for benefits in the statement of fiduciary assets and liabilities reported for that fiscal year.

For the purposes of the accompanying statement of cash flows, the enterprise fund considers all highly liquid investments with maturities of three months or less when purchased, and their equity in the State Pool to be cash equivalents.

Compensated Absences

All employees earn vacation at the rate of one and three-quarters working days for each month of service. Vacation days may be accumulated to a maximum of 90 days. Employees are entitled to receive cash payment for accumulated vacation upon termination. The accompanying financial statements present the cost of accumulated unpaid vacation as a liability. A reconciliation of changes in compensated absence liabilities for accumulated vacation is as follows for the year ended June 30, 2010:

	Enterprise Fund
Balance at beginning of year	$ 186,110
Additions	88,627
Reductions	(102,080)
Balance at end of year	172,657
Less current portion	(35,767)
	$ 136,890

All employees earn sick leave credits at the rate of one and three-quarters working days for each month of service. Sick leave credits may be accumulated without limit. Sick leave can be taken only in the event of illness and is not convertible to pay upon termination of employment. Accordingly, no liability for unpaid sick leave credits is reported in the accompanying financial statements. However, a Trust Fund employee who retires or leaves government service in good standing with sixty days or more of unused sick leave is entitled to additional service credit in the Employees' Retirement System of the State of Hawaii. Accumulated sick leave as of June 30, 2010, relating to the Trust Fund approximated $384,855.

Receivables

Receivables consist primarily of amounts due from employers and employees for health benefits premium contributions, as well as amounts due from individuals for Medicare Part B reimbursements. The employee receivables are reported as net receivables and were based on management's estimate of amounts considered collectible. Management considered receivables outstanding for more than 60 days by employees who are no longer employed by State or Counties to be uncollectible. An allowance for employer receivables is not considered necessary based on past collection experience. The Medicare reimbursement receivables from individuals are reported as net receivables and were based on management's estimate of amounts considered collectible. Management considered receivables from individuals who are deceased and do not have a surviving spouse enrolled in Medicare Part B to be uncollectible.

Risk Management

The Trust Fund is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; natural disasters; and injuries to employees. A liability for a claim for a risk of loss is established if information indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss is reasonably estimable.

Benefits Claims Expense and Cost

The benefits claims expense reported in the enterprise fund relates to the self-funded medical and prescription drug plans and includes the ultimate net cost of all reported claims incurred through June 30, 2010, for active employee healthcare benefits. The benefits claims expense also includes an additional estimate for unreported claims that have been incurred as of June 30, 2010. The cost of benefits claims for retirees, which also include provisions for unreported claims, are reported as a component of benefit claims payable in the agency fund.

Management has made certain assumptions based on currently available information and industry statistics in determining the benefits claims expense. Accordingly, the ultimate costs may vary significantly from the estimated amounts reported in the financial statements. Management believes that, given the inherent variability in benefits claims expense, such aggregate liabilities are within a reasonable range of adequacy. Such estimates are based on estimated claims cost reported prior to June 30, 2010, and estimates (based on actuarial projections of historical loss development) of claims cost incurred but not reported. Reserves are continually reviewed and adjusted as experience develops or new information becomes known; such adjustments are charged to net assets as incurred for active employees. Rebates receivable are recorded in the period that the claim is paid and is netted against the cost of the claim.

Management recorded its best estimate for the obligation of unpaid claims of $38,334,060 for active employees and $12,867,761 for retirees as of June 30, 2010, based on the Trust Fund's consulting actuary's estimate for the liability for unpaid claims. These amounts include administrative fees payable to the contracted plan administrator for services provided and benefit claims incurred as of June 30, 2010.

Carrier Payment Methodology

Premiums paid to the carriers are calculated on a monthly basis by multiplying the total number of active employees and retirees enrolled in the various plans on the last day of the month by the premium rates set forth in the contract agreements, whereas employer and employee billings are calculated on a semi-monthly basis. As a result, the Trust Fund recognizes a gain or loss between the total premiums actually collected from the employers and employees and the total premiums actually paid to the carriers. For the year ended June 30, 2010, the Trust Fund recognized losses of approximately $101,005 and $89,570, related to active employees and retirees, respectively.

HRS Section 87A does not require the Trust Fund to return insurance carrier refunds, rate credits, interest income and other earnings in excess of funds used to stabilize health benefits plan or long-term care benefits plan costs to the State General Fund and the respective counties. In addition, HRS Section 87A does not require the Trust Fund to return insurance carrier refunds, rate credits and other earnings, as authorized by the Board, to identifiable employees who participated in ascertainable years that created the refund or credit. Accordingly, the Trust Fund recognizes the gains as increases in gain/loss on carrier payment methodology and related receivable as other receivables held by insurance companies.

Administrative Fees

The Trust Fund assesses and collects administrative fees from employers to support the activities of the Trust Fund. The administrative fees are assessed each pay period and vary depending upon the type of bargaining agreements. For the year ended June 30, 2010, the administrative fees charged to participating agencies to administer the plans was $3,019,049 and $2,097,983 for active employees and retirees, respectively. These amounts are recognized as revenues in the enterprise fund, as all administrative expenses are recognized in the enterprise fund.

Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(3) CASH AND INVESTMENTS

As of June 30, 2010, the Trust Fund's cash and investments were distributed and reported in the financial statements as follows:

	2010		
	Enterprise Fund	Agency Fund	Total
Cash and cash equivalents:			
Certificates of deposit	$ -	$ 55,552,264	$ 55,552,264
Equity in the State Pool	-	51,889,100	51,889,100
Repurchase agreements	-	77,629,826	77,629,826
Total	$ -	$ 185,071,190	$ 185,071,190

Investments Authorized by the State's Investment Policy – The Trust Fund utilizes the State of Hawaii's Treasury Investment Policy (Investment Policy). Legally authorized investments include obligations of or guaranteed by the U.S. government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, student loan resource securities (including auction rate securities, asset backed securities, program revenue notes and bonds, securities issued pursuant to Rule 144A of the Securities Act of 1933), money market funds, repurchase agreements with federally-insured financial institutions, commercial paper and banker's acceptances. At June 30, 2010, in addition to the State Pool, the Trust Fund was invested in negotiable certificates of deposit and repurchase agreements, which had the following limitations per the State's Investment Policy:

Investment Type	Maximum Percentage of Portfolio	Maximum Investment in One Issuer	Maximum Investment by Issue (Position Limit per Issue)	Maximum Maturity
Negotiable certificate of deposit	Up to 50%	Up to 50%	5%	5 years
Repurchase agreement	Up to 70%	Up to 70%	10%	5 years

State Treasury Cash and Investment Pool - The State Director of Finance is responsible for safekeeping of all monies paid into the State Treasury (cash pool). The Director of Finance may invest any monies of the State, which in the Director's judgment are in excess of the amounts necessary for meeting the immediate requirements of the State. Cash is pooled with funds from other State agencies and departments and is invested in accordance with the State Investment Policy. Cash accounts that participate in the State Pool accrue interest based on the weighted average cash balances of each account. The weighted average maturity of the cash pool at June 30, 2010, was 154 days.

Interest Rate Risk – Interest rate risk is the risk that changes in the market rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. As a means of limiting its exposure to fair value losses arising from rising interest rates, the State's Investment Policy generally limits maturities on investments to not more than five years from the date of investment. As of June 30, 2010, the Trust Fund had monies invested short-term in the State Pool, negotiable certificates of deposit and repurchase agreements all with original maturities of less than three months.

Credit Risk – Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The State's Investment Policy limits investments in state and U.S. Treasury securities, time certificates of deposit, U.S. government or agency obligations, repurchase agreements, commercial paper, bankers' acceptance, and money market funds and student loan resources securities maintaining a rating of AAA. As of June 30, 2010, the State Pool and the repurchase agreements have not been rated by a nationally recognized statistical rating organization.

The State Pool as of June 30, 2010, included auction rate securities collateralized by student loans. During 2008, a number of these auctions failed and companies without the ability to hold such securities until maturity have taken significant losses. During the year ended June 30, 2010, the State experienced a favorable change in the fair value of its investments in the auction rate securities due to improved market conditions, and recorded an increase in fair value. The Trust Fund's allocated share of the increase was $3,010,221 for the year ended June 30, 2010, of which $1,806,133 and $1,204,088 was allocated to the enterprise fund and agency fund, respectively, resulting in a total cumulative decrease of $1,491,756 as of June 30, 2010. These adjustments were recorded as an increase of cash and cash equivalents and interest income and other in the enterprise fund and cash and cash equivalents and amounts held on behalf of employers for benefits in the agency fund.

Custodial Credit Risk – For an investment, custodial credit is the risk that, in the event of the failure of the counterparty, the Trust Fund will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Trust Fund's investments are held at broker/dealer firms, which are protected by the Securities Investor Protection Corporation (SPIC) up to a maximum amount. In addition, excess-SPIC coverage is provided by the firms' insurance policies. Furthermore, the State requires institutions to set aside in safekeeping, certain types of securities to collateralize repurchase agreements. The State Treasury monitors the market values of these securities on behalf of the Trust Fund and obtains additional collateral when appropriate.

Concentration of Credit Risk – The State's Investment Policy provides guidelines for the portfolio diversification by placing limits on the amount the Trust Fund may invest in any one issuer, types of investment instruments, and position limits per issue of an investment instrument. At June 30, 2010, the Trust Fund's investment concentration was as follows:

	2010	
Investment Type/Issuer	Investment Type - Percentage of Portfolio	One Issuer of Investment Instrument - Percentage of Portfolio
Repurchase agreements	60%	
Bank of Hawaii		47%
First Hawaiian Bank		13%

(4) CAPITAL ASSETS

The enterprise fund capital asset activity for the year ended June 30, 2010, was as follows:

	Balance at July 1, 2009	Amounts Reclassified from Agency Fund as July 1, 2009	Balance at July 1, 2009 Restated	Increases	Decreases	Balances at June 30, 2010
Capital assets, not being depreciated						
Software development in progress	$ 3,819,643	$ 2,546,431	$ 6,366,074	$ 1,578,309	$ (7,944,383)	$ -
Capital assets being depreciated						
Office furniture and equipment	2,538,877	1,715,906	4,254,783	14,155	-	4,268,938
Software	-	-	-	9,369,750		9,369,750
Less accumulated depreciation	(2,439,682)	(1,626,459)	(4,066,141)	(914,118)	-	(4,980,259)
Total capital assets, being depreciated net	99,195	89,447	188,642	8,469,787	-	8,658,429
Capital assets, net	$ 3,918,838	$ 2,635,878	$ 6,554,716	$ 10,048,096	$ (7,944,383)	$ 8,658,429

As of June 30, 2010, capital asset balances previously recorded in the agency fund were reclassified to the enterprise fund. The Trust Fund has developed an expense allocation to recover a portion of depreciation expense from the agency fund for use of the capital assets in administering the agency fund. Approximately 41% of the depreciation expense for fiscal year 2010 was recovered from the agency fund as part of the administrative fee charged to the agency fund.

(5) HEALTH AND LIFE INSURANCE BENEFIT CONTRACTS

The Trust Fund's primary purpose is to provide employee-beneficiaries, retiree-beneficiaries and dependent-beneficiaries with a health benefits plan and group life insurance. To effectuate that purpose, the Trust Fund requested proposals in August 2006 and awarded multi-year health and life insurance benefit contracts commencing July 1, 2007 and continuing through June 30, 2009 and subsequently exercised its option to extend contracts for an additional two year period through June 30, 2011.

Individual carriers / administrators are addressed below. The plans were offered with 3 different financial arrangements:

- Self funding: The medical PPOs with Health Management Associates (HMA) and Hawaii Medical Service Association (HMSA) acting as third party administrators (TPA), medical health maintenance organization (HMO), high deductible health plan (HDHP) and supplemental with HMSA, and the prescription drug coverage with NMHC (now informed Rx) as administrator are all self funded plans. Rates are experience rated and are set by the Trust Fund Board acting on the advice of the consultant/actuary. Due to the size of the pool there is no stop loss insurance associated with these plans. The Trust Fund pays administrative fees to the TPAs and pays actual claim costs as claims are paid. If claims are less than the amount projected and included in the premium collection from employers and employee-beneficiaries, surplus funds remain in the Trust Fund. In addition, prescription drug rebates are received from informedRx 6 to 9 months after they are realized.

- Fully insured: The Kaiser Basic and Comprehensive HMO plans and the Royal State Chiropractic Plan are all fully insured. Premiums are received from employers and paid to the carriers. There is no additional risk to the Trust Fund or funds to be paid to the Trust Fund. Rates are set by Kaiser and Royal State.

- Fully insured with Retrospective Risk Sharing and Risk Sharing: The Hawaii Dental Service (HDS) and Vision Services Plan (VSP) plans are funded through a fully insured retrospective risk sharing arrangement. Rates are set by HDS and VSP using the plans' experience. Full premium is collected from employers and 95% (HDS & VSP) is paid to the carriers. At the end of the year, if claims and retention exceed the reduced premium paid, the Trust Fund will pay the carriers the amount of the excess up to the withheld five percent (5%). The annual accounting for active employees and retirees is maintained separately. As such, the premium surplus of one group cannot be used to offset the underwriting loss of another group. Upon expiration or termination of the contract, any premium surplus will be refunded to the Trust Fund and any underwriting losses will not be paid by the Trust Fund. The Royal State Dual Coverage Supplemental Plan is funded through a fully insured risk sharing arrangement and is similar to the HDS and VSP plans except there are no retrospective premiums.

<u>Health Maintenance Organization – Closed Panel HMO</u>

The Trust Fund entered into a contract with Kaiser Foundation Health Plan, Inc. (Kaiser) to provide active employees and retirees with HMO benefits for the period July 1, 2007 through June 30, 2009 and subsequently exercised its option to extend the contracts for an additional two years through June 30, 2011. The HMO does not use experience rating for setting the premium rates. Accordingly, there is no premium surplus or underwriting loss.

Medical and Prescription Drug Benefits

The Trust Fund entered into a contract with the HMSA and HMA to provide claims administration services for active employees and retirees for medical plans for the period July 1, 2007 through June 30, 2009, and subsequently exercised its option to extend the contract for an additional two years through June 30, 2011. The plans include a 90/10 PPO with HMA and a 90/10 PPO (July 1, 2009 through January 31, 2010), 80/20 PPO (effective February 1, 2010), HMO, HDHP and Supplemental Plan with HMSA. The amounts paid for claims and administrative services to HMSA and HMA are reconciled with the payments made by HMSA and HMA and any remaining surplus or deficit will be remitted to or owed by the Trust Fund. As of June 30, 2010, amounts held by HMSA were $28,859 for active employees and $24,584 for retirees.

The Trust Fund entered into a contract with informedRx for the period July 1, 2007, through June 30, 2009, and subsequently exercised its option to extend the contract for an additional year through June 30, 2010. The contract was extended again for an additional year through June 30, 2011. The Trust Fund's contract with informedRx entitles the Trust Fund to rebates from pharmaceutical manufacturers related to claims paid by the Trust Fund and processed by informedRx. As of June 30, 2010, rebates receivable from informedRx were $1,658,814 for active employees and $3,385,529 for retirees.

Vision Care Benefits

The Trust Fund entered into a contract with VSP for the period July 1, 2007 through June 30, 2009 and subsequently exercised its option to extend the contract for an additional two years through June 30, 2011. The contracts include a five percent (5%) retrospective premium agreement for both active employees and retirees. Under these agreements, the Trust Fund will pay VSP ninety-five percent (95%) of the premiums due each month.

At the end of the plan year, if claims and retention exceed 95% of the premiums due for the plan year, the Trust Fund will pay VSP the amount of the excess up to the withheld 5%. Since VSP is still allowed to receive the retrospective premium if they experience losses for the plan year based on the final accounting, a payable to VSP was recorded. At June 30, 2010, the Trust Fund's retrospective premium payable was $254,142 and $148,338 for active employees and retirees, respectively.

Dental Benefits

The Trust Fund entered into a contract with HDS for the period July 1, 2007, through June 30, 2009, and subsequently exercised its option to extend the contract for an additional two years through June 30, 2011. The contracts include a five percent (5%) retrospective premium agreement for both active employees and retirees. Under these agreements, the Trust Fund will pay HDS ninety-five percent (95%) of the premiums due each month.

At the end of the plan year, if claims and retention exceed 95% of the premiums due for the plan year, the Trust Fund will pay HDS the amount of the excess up to the withheld ten percent (5%). Since HDS is still allowed to receive the retrospective premium if they experience losses for the plan year based on the final accounting, a payable to HDS was recorded. At June 30, 2010, the

Trust Fund's retrospective premium payable was $0 and $866,044 for active employees and retirees, respectively.

Life Insurance Benefits

The Trust Fund entered into a contract with Standard Insurance Company (Standard) to provide term life insurance benefits to all eligible active employees and retirees for the period July 1, 2007 through June 30, 2009 and subsequently exercised its option to extend the contract for an additional year through June 30, 2010. The contract was extended again for an additional year through June 30, 2011. The amounts paid for claims and administrative services are reconciled with the payments made to Standard and any remaining surplus will be refunded to the Trust Fund and any underwriting losses will not be paid by the Trust Fund.

Dual-Coverage Medical and Prescription Drug Benefits

The Trust Fund entered into a contract with Royal State National Insurance Company, Ltd. (RSN) to provide active employees with dual-coverage medical and prescription drug benefits for the period July 1, 2007 through June 30, 2009 and subsequently exercised its option to extend the contract for an additional two years through June 30, 2011. The amounts paid for claims and administrative services are reconciled with the payments made to RSN and any remaining surplus will be refunded to the Trust Fund and any underwriting losses will not be paid by the Trust Fund. As of June 30, 2010, amounts held by RSN were $2,837 for active employees and $0 for retirees.

<u>All Contracts</u>

The following is a summary of the of premium reserves held by insurance companies, rebates receivable, retrospective premiums payable, and premiums payable balances by insurance company at June 30, 2010:

	Active Employees	Retirees
Other receivables held by insurance companies		
RSN	$ 2,837	$ -
HMSA	28,859	24,584
	$ 31,696	$ 24,584
Rebates receivable		
Receivable from informed Rx	$ 1,658,814	$ 3,385,529
Receivable from HMSA	97,153	-
	$ 1,755,967	$ 3,385,529
Retrospective premiums payable:		
HDS - dental contract	$ -	$ 866,044
VSP - vision contract	254,142	148,338
	$ 254,142	$ 1,014,382
Premiums payable		
HDS	$ 4,198,739	$ 1,959,347
Kaiser Hawaii	5,077,699	3,091,172
ROYAL DUAL	137,737	-
VSP	398,082	529,930
Standard	221,977	136,051
COBRA payable · HDS	9,783	-
COBRA payable · Royal	37	-
COBRA payable · Kaiser	2,431	-
COBRA payable · HMA	(19,795)	-
	$ 10,026,690	$ 5,716,500

(6) BENEFIT CLAIMS EXPENSE

Beginning July 1, 2007, the Trust Fund offered self-funded medical and prescription drug plans, administered by Hawaii Medical Service Association (HMSA), Health Management Associates (HMA), and National Medical Health Card Systems (NMHCS) (now informed Rx) under contracts for the period July 1, 2007 through June 30, 2009, which were subsequently extended through June 30, 2011. Under the self-funded arrangements, the contract administrators provide the Trust Fund provider networks, claims processing, cost containment and other services. Instead of premiums, the Trust Fund pays administrative fees to the contractor for the services rendered and reimburses the contractor for claims paid. Activity in the liability for unpaid benefit claims expense related to the self-funded medical and prescription drug plans is as follows for the years ended June 30, 2009 and 2010:

	Active employees	Retirees	Total
Balance at July 1, 2008	$ 36,951,791	$ 9,215,230	$ 46,167,021
Current year claims and changes in estimates	258,521,518	173,267,524	431,789,042
Contractor processing administrative fees related to current year	13,427,564	14,004,110	27,431,674
Paid during current year	(262,907,460)	(182,168,597)	(445,076,057)
Balance at June 30, 2009	$ 45,993,413	$ 14,318,267	$ 60,311,680
Balance at July 1, 2009	$ 45,993,413	$ 14,318,267	$ 60,311,680
Current year claims and changes in estimates	233,011,952	161,907,925	394,919,877
Contractor processing administrative fees related to current year	11,960,034	13,756,828	25,716,862
Paid during current year	(252,631,339)	(177,115,259)	(429,746,598)
Balance at June 30, 2010	$ 38,334,060	$ 12,867,761	$ 51,201,821

Below is a summary of benefit claims payable by carrier at June 30, 2010:

	Active Employees	Retirees
Benefit claims payable:		
Benefit claims - HMA	$ 603,211	$ 3,152
Benefit claims - HMSA	13,515,719	7,342,185
Benefit claims - InformedRx	1,969,864	4,536,114
IBNR for Self Funded Plans	21,301,000	-
Admin Fee - HMA	94,529	1,719
Admin Fee - HMSA	849,062	822,051
Admin Fee - informedRx	675	162,540
	$ 38,334,060	$ 12,867,761

According to the terms of contracts with HMSA and informed Rx, the Trust Fund was required to make a deposit to cover estimated claims costs for the self-funded medical and prescription drug plans. The deposits held by the carriers for the self-funded medical and prescription drug plans as of June 30, 2010 is as follows:

	Active Employees	Retirees	Total
HMSA – Medical and drug contract	$ 6,300,000	$ 3,700,000	$ 10,000,000
InformedRx (formerly NHMCS) -			
Drug contract	3,008,000	6,392,000	9,400,000
HMA - Medical contract	2,200,680	156,076	2,356,756
	$ 11,508,680	$ 10,248,076	$ 21,756,756

(7) SUMMARY OF CONTRIBUTIONS AND PRE-FUNDED DEPOSITS

The employer and employee contributions recognized and deposits received for the year ended June 30, 2010, were as follows:

Required contributions	Active employees	Retirees	Total
Employer			
State of Hawaii	$ 127,245,376	$ 224,625,023	$ 351,870,399
City & County of Honolulu	39,531,299	57,160,226	96,691,525
County of Hawaii	11,078,480	12,483,917	23,562,397
County of Maui	11,446,612	9,682,157	21,128,769
County of Kauai,			
including Department of Water	5,298,434	6,005,463	11,303,897
Board of Water Supply – Honolulu	2,431,661	4,773,029	7,204,690
County of Hawaii - Department of Water	807,205	663,719	1,470,924
	197,839,067	315,393,534	513,232,601
Employee	158,967,090	1,114,511	160,081,601
	356,806,157	316,508,045	673,314,202
Pre-funded deposits			
Employer			
County of Hawaii	-	15,700,000	15,700,000
County of Maui	-	12,676,000	12,676,000
County of Kauai,			
including Department of Water	-	7,661,750	7,661,750
Board of Water Supply – Honolulu	-	4,000,000	4,000,000
County of Hawaii - Department of Water	-	1,300,000	1,300,000
	-	41,337,750	41,337,750
Subtotal – required and pre-funding deposits	356,806,157	357,845,795	714,651,952
Less: amounts received for administrative fees	(3,019,049)	(2,097,983)	(5,117,032)
Total contributions and deposits			
received for benefit payments	$ 353,787,108	$ 355,747,812	$ 709,534,920

The required contributions include both contributions for self-insured and fully-insured plans. The self-insured contributions are reported as operating revenues in the statement of revenues, expenses and changes in net deficit for the enterprise fund. The contributions related to the fully-insured plans are included as a component of the benefit claims payable on the statement of net assets for the enterprise fund and the statement of fiduciary assets and liabilities for the agency fund. Contributions related to the fully-insured plans were $103,511,078 and $62,115,956 for the enterprise fund and agency fund, respectively.

As a result of plan operations in the current year, the Trust Fund utilized previously built-up reserves to cover the cost of healthcare benefits resulting in a transfer from the agency fund to the enterprise fund of $2,198,481 for the year ended June 30, 2010.

(8) RETIREMENT BENEFITS

A. Employees' Retirement System

Plan Description

All eligible employees of the State are required by Chapter 88 of the Hawaii Revised Statutes to become members of the Employees' Retirement System of the State of Hawaii (ERS), a cost-sharing multiple-employer public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits. The ERS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information for ERS. That report may be obtained by writing to the ERS at 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813.

The ERS consists of a contributory plan and a noncontributory plan. Employees covered by Social Security on June 30, 1984 were given the option of joining the noncontributory plan or remaining in the contributory plan. All new employees hired after June 30, 1984, who are covered by Social Security, are generally required to join the noncontributory plan. Both plans provide a monthly retirement allowance based on the employee's age, years of credited service, and average final compensation (AFC). The AFC is the average salary earned during the five highest paid years of service, including the payment of salary in lieu of vacation, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after this date is based on the three highest paid years of service excluding the payment of salary in lieu of vacation. Vesting requirements for the contributory and noncontributory plans are five years and ten years, respectively. All contributions, benefits and eligibility requirements are governed by Chapter 88.

On July 1, 2006, a new hybrid contributory plan became effective pursuant to Act 179, SLH of 2004. Members in the hybrid plan are eligible for retirement at age 62 with 5 years of credited service or age 55 and 30 years of credited service. Members will receive a benefit multiplier of 2% for each year of credited service in the hybrid plan. The benefit options are similar to the current contributory plan. Approximately 58,000 current members, all members of the noncontributory plan and certain members of the contributory plan, are eligible to join the new hybrid plan. Most of the new employees hired from July 1, 2006 are required to join the hybrid plan.

Funding Policy

Police officers, firefighters, investigators of the department of the prosecuting attorney and the attorney general, narcotics enforcement investigators, and public safety investigators are required to contribute 12.2% in 2010 of their salary. For all other employee groups, the average weighted effective contribution rate is 6.05% of pay. The actuarial cost or funding method used to calculate the total employer contribution required is the entry age normal actuarial cost method. Under this method, the employer contribution rates are a fixed percentage of compensation, including normal cost plus amounts required to pay for the unfunded actuarial accrued liability.

The employer contribution rate for June 30, 2010 was 15%.

The Trust Fund's share of the aggregated pension expense was approximately $169,800, $186,000 and $151,000 for the years ended June 30, 2010, 2009 and 2008, respectively, and the annual expense is included in the financial statements.

Refer to the State's basic financial statements for information regarding required supplementary information regarding the funding progress and plan information for State Employees.

B. Postemployment Health Care and Life Insurance Benefits

Plan Description

In addition to providing pension benefits, the State, pursuant to HRS Chapter 87A, provides certain health care and life insurance benefits to all qualified retirees under an agent multiple-employer defined benefit plan. The plan's participating employers include the State and Counties of Honolulu, Hawaii, Maui and Kauai (Counties).

For employees hired before July 1, 1996, and who retire with ten or more years of credited service, the State and the Counties pay 100% of the base monthly contribution set forth under HRS Section 87A- 33(b) for retirees enrolled in Medicare or non-Medicare health benefits plans. For retirees with fewer than ten years of credited service, the State and Counties pay 50% of the base monthly contribution set forth under HRS Section 87A-33(b).

For employees hired after June 30, 1996 but before July 1, 2001, and who retire with fewer than 10 years of service, the State and Counties make no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State and Counties pay a monthly contribution equal to 50% of the base monthly contribution set forth under HRS Section 87A-33(b). For employees retiring with at least 15 years but fewer than 25 years of service, the State and Counties pay a monthly contribution equal to 75% of the base monthly contribution set forth under HRS Section 87A-33(b). For employees retiring with at least 25 years of service, the State and Counties pay a monthly contribution equal to 100% of the base monthly contribution set forth under HRS Section 87A-33(b).

The contribution rates for employees hired after June 30, 2001, are consistent with the contribution rates for those hired after June 30, 1996, but only self plan base monthly contribution rates are applied. Those retirees may elect to enroll additional dependents, but they must pay the additional cost.

As of July 1, 2009, the date of the most recent actuarial valuation the plan membership was as follows:

	Retirees (including Surviving Spouse) Receiving Benefits	Deferred Vested Members not yet Receiving Benefits	Active Employees	Total
Employer:				
State of Hawaii	28,449	3,407	38,534	70,390
City & County of Honolulu	6,286	637	8,751	15,674
County of Hawaii	1,290	127	2,327	3,744
County of Maui	1,051	166	2,390	3,607
County of Kauai, including Department of Water	633	85	1,076	1,794
Board of Water Supply – Honolulu	564	43	549	1,156
County of Hawaii - Department of Water Supply	78	-	181	259
	38,351	4,465	53,808	96,624

Funding Policy

Contributions to the plan are made by both the participating employers and employees. Contribution amounts are established by statute and are currently based on the pay-as-you-go amounts billed by the Trust Fund to the employers; however, employers may elect to make additional deposits based on their respective actuarial valuations. The retirees are responsible to pay the difference if the base contribution is less than the cost of the monthly premium. The current contributions are not sufficient to provide adequate assets to pay benefits when due in accordance with the requirements of GASB 43.

The participants required contribution to the Trust Fund is based on the pay-as-you-go basis and the actuarial determined annual required contribution (ARC) amount for the year ended June 30, 2010, based on the July 2009, actuarial valuations, were as follows:

	Required Contribution for June 30, 2010 (pay-as-you-go basis)	ARC for June 30, 2010	ARC as a Percentage (%) of Covered Payroll
Employer:			
State of Hawaii	$ 224,625,023	$ 806,981,000	41.9%
City & County of Honolulu	57,160,226	113,135,000	20.3%
County of Hawaii	12,483,917	25,046,000	18.8%
County of Maui	9,682,157	21,800,000	16.1%
County of Kauai, including Department of Water	6,005,463	11,926,000	18.1%
Board of Water Supply – Honolulu	4,773,029	7,837,000	23.7%
County of Hawaii - Department of Water Supply	663,719	1,607,000	17.0%
	$ 315,393,534	$ 988,332,000	

Beginning in fiscal year 2008, the Trust Fund receives and holds deposits from participating employers to pre-fund retiree benefits on behalf of the employees in a separate account in the agency fund and allocates any interest earned related to those the pre-funding deposits based on accumulated amounts to date. These deposits do not meet the criteria of a contribution to the other postemployment benefits plan as the plan does not meet the criteria of a trust fund under GASB 43. The cumulative deposits and interest held by the Trust Fund in the agency fund for pre-funding are as follows as of June 30, 2010:

Board of Water Supply – Honolulu	$ 7,249,412
County of Hawaii	44,560,764
County of Maui	25,116,132
County of Kauai, including Department of Water	14,947,572
Hawaii County Department of Water Supply	3,166,173
City & County of Honolulu	40,142,037
	$ 135,182,090

Each participating employer is required to disclose additional information with regard to funding policy, the employers' annual OPEB cost and contributions made, the funded status and funding progress of the employer's individual plan, and actuarial methods and assumptions used.

Annual OPEB Cost and Net OPEB Obligation Related to the Trust Fund

The employees that administer the Trust Fund are employees of the State. The Trust Fund's annual other postemployment (OPEB) cost (expense) is allocated by the State based on the Trust Fund's proportionate share of contributions for postemployment health benefits and was calculated at 0.0398% of the State's annual required contribution (ARC) for the year ended June 30, 2010. The ARC is an amount actuarially determined in accordance with GASB 45, which was implemented effective July 1, 2007.

The following table shows the components of the annual OPEB cost, the amount contributed to the plan, and changes in the Trust Fund's net OPEB obligation for the year ended June 30, 2010.

Annual required contribution	$ 272,953
Interest on net OPEB obligation	8,920
Adjustment to annual required contribution	(8,116)
Annual OPEB cost	273,757
Contributions made	(75,991)
Increase in net OPEB obligation	197,766
Net OPEB obligation at beginning of year	345,924
Net OPEB obligation at end of year	$ 543,690

The percentage of annual OPEB cost contributed was 27.0%, 36.1% and 35.9% for the years ended June 30, 2010, 2009 and 2008, respectively.

Actuarial Methods and Assumptions Used in the State's Actuarial Valuation

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	7/1/2009
Actuarial cost method	Entry age normal
Amortization method	Level percentage of payroll, open
Amortization period	30 years
Actuarial assumptions:	
Investment rate of return	4%
Healthcare cost trend rate (1):	
Medical and prescription drug	10.5% initial; 5% ultimate
Dental	6% initial; 4% ultimate
Vision	4% initial; 3% ultimate
Medicare Part B	14.6% initial; 5% ultimate
Projected salary increases	3.5%

(1) Includes an inflation assumption of 3%.

Refer to the State's basic financial statements for information regarding required supplementary information regarding the funding progress and plan information for State Employees.

(9) COMMITMENTS AND CONTINGENCIES

Deferred Compensation

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all State employees, permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All plan assets are held in a trust fund to protect them from claims of general creditors. The State has no responsibility for loss due to the investment or failure of investment of funds and assets in the plan, but does have the duty of due care that would be required of an ordinary prudent investor. Accordingly, the assets and liabilities of the State's deferred compensation plan are not reported in the State's or Trust Fund's financial statements.

Litigation

On June 30, 2006, a class action lawsuit was brought in the First Circuit Court, State of Hawaii, by certain State and county retirees against the Trust Fund, the Trust Fund's board of trustees, and the State ("collectively "State defendants"), as well as various county governments that participate in the Trust Fund's health benefit plans. The plaintiffs' amended complaint alleges various claims based on an argument that the Trust Fund is constitutionally, statutorily, and contractually required to provide health benefit plans that provide retirees and their dependents with benefits that are substantially equal to those provided to active employees and their dependents. In addition, the plaintiffs claim that the Trust Fund's failure to provide substantially equal health benefit plans to retirees and their dependents was negligent. The plaintiffs seek declaratory and injunctive relief, damages, and attorneys' fees and costs. The damages sought appear to be amounts that the plaintiffs (and their class) have paid for health benefits, which they would not have paid had their plans been equivalent to the Trust Fund's active employee plans. The defendants filed motions to dismiss the plaintiffs' complaint. The judge decided that the Trust Fund had primary jurisdiction over issues involved in the plaintiffs' claims and stayed this action pending referral of those issues to the Trust Fund.

In May and June 2007, the plaintiffs filed a petition with the Trust Fund's board of trustees seeking a declaratory ruling regarding certain issues raised by their lawsuit. The Trust Fund's board of trustees held a hearing on the plaintiffs' petition under the Trust Fund rules and Chapter 91 of the HRS. After the hearing, the Trust Fund's board of trustees issued Findings of Fact, Conclusions of Law, and Order. The plaintiffs filed an appeal for judicial review of the Findings of Fact, Conclusions of Law, and Order under HRS §91-14. Plaintiffs appealed the Trust Fund's rulings to the First Circuit Court, State of Hawaii. After briefing and oral argument, the First Circuit Court overturned the Trust Fund's Board's rulings. The State and the Trust Fund's Board appealed the First Circuit Court's decision. On March 26, 2010, the Hawaii Supreme Court affirmed in part and reversed in part the First Circuit Court's decision. The Hawaii Supreme Court held that the First Circuit Court: (1) did not err in concluding that a retired state and county government employee's health benefits are protected by Article XVI, Section 2 of the Hawaii Constitution as "accrued benefits," and (2) erred by concluding that HRS Chapter 87A requires that postemployment health benefits reasonably approximate those of active workers. On March 2, 2011, Judge Patrick Border of the First Circuit Court, State of Hawaii, heard and granted Plaintiffs' motion for class action certification. The class certified was all individuals who began working for the Territory of Hawaii, State of Hawaii, or any political subdivision thereof, prior to July 1, 2003, and who qualify as a retired employee-beneficiary and/or whose dependent qualifies as a dependent-beneficiary as those terms are defined in sections 87A-1 and 87A-21 of the Hawaii Revised Statutes.

The parties are currently engaged in discovery. No trial date has yet been set. State Defendants intend to continue to vigorously defend against Plaintiffs' claims in this lawsuit. The outcome of this lawsuit cannot be determined and no amount has been recorded in the financial statements as of or for the year ended June 30, 2010.

<u>Kono, et al. v. Abercrombie, Civil No. 10-1-1966-09 KKS</u>

On September 14, 2010, the Hawaii State Teachers Association Voluntary Employees Beneficiary Association Trust (VEBA Trust) and two participants in the VEBA Trust health plans filed a Complaint against the State of Hawaii (State) alleging: (1) The State diminished and impaired accrued health benefits of the active and retired teachers participating in the VEBA Trust health plans in violation of Article XVI, Section 2 of the Hawaii Constitution, by enacting Act 106, Session Laws of Hawaii 2010 (Act 106) and transferring the VEBA members to the Trust Fund and/or reassigning the administration of the VEBA Trust health benefits plans from the VEBA Trust to the Trust Fund; and (2) the State had taken $3.96 million in surplus funds from the VEBA Trust and this similarly diminished or impaired the VEBA members' accrued health benefits in violation of Article XVI, Section 2. Plaintiffs also alleged breach of contract by the State, and that the taking of the $3.96 million constituted unjust enrichment.

On October 12, 2010, the State filed a motion for judgment on the pleadings and to dismiss the Complaint in its entirety. On November 4, 2010, Plaintiffs filed a motion for preliminary injunction to maintain the status quo and prevent the transfer of the VEBA members to the Trust Fund.

Both the State's motion and Plaintiffs' motion were heard by the Honorable Karl K. Sakamoto, First Circuit Court, on December 7, 2010. While denying both motions, Judge Sakamoto held that the VEBA members did not have an accrued benefit in staying in the VEBA Trust health plans and that the transfer of VEBA members back to the Trust Fund health plans under Act 106 did not violate Article XVI, Section 2. The court further held that pursuant to Article XVI, Section 2, the VEBA members had an accrued benefit in the standard of coverage that they enjoyed in the VEBA Trust health plans and were entitled to maintain the same standard of coverage when they were transferred back to the Trust Fund. Regarding the $3.96 million, Judge Sakamoto found that to the extent that the surplus funds were part of the accrued benefits of the VEBA members who paid into the surplus, "the appropriate remedy is to allow the taking of the VEBA Trust surplus but that such amounts to be set aside to help ensure that the VEBA members can maintain their standard of accrued benefits."

On March 15, 2011, pursuant to his oral ruling, Judge Sakamoto issued an order denying the State's motion for judgment on the pleadings, an order denying Plaintiffs' motion for preliminary injunction, and a final judgment. The State timely filed an appeal of the two orders and the final judgment. Recently, the Hawaii Intermediate Court of Appeals dismissed the appeal because the form of Judge Sakamoto's final judgment did not comply with applicable requirements. State Defendants intend to pursue an appeal of Judge Sakamoto's orders and to continue to vigorously defend against Plaintiffs' claims in this lawsuit. The outcome of this lawsuit cannot be determined and no amount has been recorded in the financial statements as of or for the year ended June 30, 2010.

(10) RISK MANAGEMENT

The Trust Fund is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation.

The State has insurance policies with a variety of insurers for property coverage for its buildings, contents and equipment. The coverage includes loss from fire, boiler & machinery, terrorism coverage, as well windstorm, flood, tsunami and earthquake damage. The State also purchases excess liability insurance, medical insurance, faithful performance of duty, and depositors & forgery insurance for state employees, but is self-insured for other perils, including workers' compensation and automobile losses. Expenditures for workers' compensation, automobile losses, and general liability (for amounts not covered by insurance) are appropriated annually.

The limit of loss per occurrence is $100,000,000, except for flood and earthquake which individually have a $100,000,000 annual aggregate and terrorism which is $50,000,000 per occurrence and a $50,000 deductible.

The deductible for the usual losses is $1,000,000 per occurrence. The deductible for catastrophic losses, such as windstorm, flooding, tsunami and earthquake is 3% of the value of the building, contents and equipment, subject to a $1,000,000 per occurrence minimum. The State also has a crime insurance policy for various types of fidelity coverage with a limit of loss of $10,000,000 per occurrence with a $500,000 deductible per occurrence, except for claims expense coverage which has a $100,000 limit per occurrence and a $1,000 deductible. The deductibles are usually handled by the risk management office. Losses in excess of the risk management funds and are covered by insurance are paid by the insurance companies. Losses not covered by insurance are usually paid from legislative appropriations of the State's General Fund.

Tort claims $10,000 or less and automobile claims of $15,000 per claimant are handled by the risk management office of the Department of Accounting and General Services. All other claims are handled by the Department of the Attorney General. The State has an excess liability policy which covers bodily injury and property damage liability; including automobile and public errors and omissions, and other liabilities in force with a $4,000,000 self-insured retention per occurrence. The coverage is $10,000,000 per occurrence, with individual $10,000,000 annual aggregates for certain sub-limits of coverage. Losses not covered by insurance are generally paid from legislative appropriations of the State's General Fund.

The State is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. The State generally retains the first $1 million per occurrence of property losses, the first $4 million with respect to general liability claims, and the first $500,000 of losses due to crime. Losses in excess of these retention amounts are insured with commercial insurance companies. The limit per occurrence for property losses is $100 million, except for flood and earthquake, which individually are $100 million annual aggregate and terrorism which is $50 million per occurrence. The limit per occurrence for excess liability losses is $10 million, with certain sub-limit coverage having annual aggregates of $10 million. Crime insurance has $10 million per occurrence limit of coverage. The State also has an insurance policy to cover medical malpractice risk in the amount of $25 million per occurrence and $29 million in the aggregate. The State is generally self-insured for workers' compensation and automobile claims.

The estimate reserve for losses and loss adjustment costs include the accumulation of estimates for losses and claims reported prior to fiscal year-end, nonincremental estimates on projections of historical developments) of claims incurred but not reported, and nonincremental estimates of costs for investigating and adjusting all incurred and unadjusted claims. Amounts are subject to the impact of future changes in economic and social conditions. The State believes that, given the inherent variability in any such estimates, the reserves are within a reasonable and acceptable range of adequacy. Reserves are continually monitored and reviewed, and as settlements are made and reserves adjusted, the differences are reported in current operations. A liability for a claim is established if information indicates that is probable that a liability has been incurred at the date of the basic financial statements and the amount of the loss is reasonably estimable.

In accordance with HRS 87A-25, the Trust Fund obtained additional fiduciary liability insurance with an annual aggregate for losses of $10 million and a fidelity bond to cover employee dishonesty with an annual aggregate for losses of $1 million. In addition, the Trust Fund also obtained a public officials and employment practices insurance policy to cover any wrongful acts or employment practices violation in which the Trust Fund retains the first $25,000 per occurrence and the annual aggregate for losses is $3 million.

(11) LEASE COMMITMENT

The Trust Fund's office is located in the City Financial Tower. The State Department of Accounting and General Services (Lessee) leases the Trust Fund's office from the Employees' Retirement System of the State of Hawaii (Lessor). The lease is being paid for by the Trust Fund.

The lease commenced on January 1, 2005 and expired on November 30, 2009. In December 2009, the lease was amended with an expiration date of October 31, 2014. In January 2011, the lease was amended to surrender and acquire office space. The total rentable space was reduced from 10,324 square feet to 9,555 square feet. In addition to minimum rent, the lease provides for the payment of common area maintenance charges. At June 30, 2010, the aggregated minimum rental commitment under the noncancelable operating lease is as follows:

Year ending June 30,	
2011	$ 318,000
2012	318,000
2013	318,000
2014	318,000
2015	106,000
Thereafter	-
	$ 1,378,000

The rent expense for the year ended June 30, 2010 was $314,994.

(12) RESTATEMENT

At July 1, 2009, the Trust Fund reclassified all activity related to capital assets, operating revenues and expenses and related assets and liabilities previously reported in the agency fund to the Enterprise Fund to better account for and report administrative costs to administer the Trust Fund. As a result the Enterprise Fund net assets were restated as follows:

Net deficit at July 1, 2009	$ (19,916,788)
Prepaid expenses	13,576
Capital assets	2,635,878
Vouchers and contracts payable	(135,404)
Accrued wages and employees benefits payable	(192,550)
Compensated absenses	(74,444)
Net deficit at July 1, 2009, restated	$ (17,669,732)

Another difference in presentation from the year ended June 30, 2009 to 2010 relates to the presentation of the self-insured premiums revenues and benefit claims expenses. These amounts had been previously reported net as nonoperating revenues on the statement of revenues, expenses and changes in net deficit. In the year ended June 30, 2010, that presentation was changed to reflect the amount of premium revenues as operating revenues and the amount of related benefit expenses as operating expenses. This change was as a result of GASB 10, where the risk of loss for these self-insured programs transfers from the employers to the Trust Fund.

(13) SUBSEQUENT EVENTS

Hawaii State Teacher's Association

Act 245, SLH 2005 (partially codified as HRS Chapter 87D), temporarily authorizes employee organizations to establish voluntary employees beneficiary association (VEBA) trusts to provide health benefits to state and county employees in their bargaining units outside of the Trust Fund. Act 245, SLH 2005 established a VEBA trust three-year pilot program to allow for the analysis of the costs and benefits of a VEBA trust against those of the Trust Fund. Effective March 1, 2006, the Hawaii State Teachers Association (HSTA) implemented the three-year pilot program. As a result, all active HSTA employees were enrolled in the VEBA trust and subsequently canceled from the Trust Fund's health benefit plans. Act 245 was amended by Act 294, SLH 2007 to extend the repeal date to July 1, 2009, for any VEBA implemented in March 2006. Act 5, First Special Session 2008, amended Act 245, SLH 2005 to extend the sunset date to July 1, 2010. Subsequently, Act 106, SLH 2010 extended the sunset date to December 31, 2010.

In addition, Chapter 87D of the Hawaii Revised Statutes which authorized the establishment of the VEBA, also included the option for HSTA retirees to make a one-time choice to either remain with the Trust Fund or transfer to the HSTA VEBA benefit plans. The option period was from October through November 2006. As a result, approximately 1,400 HSTA retirees transferred to the HSTA VEBA effective January 1, 2007. HSTA employees that retired on or after March 1, 2006, are required to be enrolled with the HSTA VEBA and do not have the option to enroll with the Trust Fund.

Effective January 1, 2011, the HSTA VEBA was terminated and all employees receive benefits through the Trust Fund. In December 2010, Judge Sakamoto ruled that HSTA VEBA members (actives and retirees) were entitled to the same standard of coverage in benefits when they were transitioned to the Trust Fund on January 1, 2011. The enrollment of HSTA VEBA members into these new Trust Fund-created health and other benefit plans was done solely to comply with Judge Sakamoto's ruling and does not create any constitutional or contractual right to the benefits by these plans. The State does not agree with Judge Sakamoto's ruling. If Judge Sakamoto's ruling is overturned, stayed, or modified, the Trust Fund reserves the right to move HSTA VEBA members into regular Trust Fund plans.

Auction Rate Securities Settlement

On November 23, 2010, the State and Citigroup Global Markets Inc. (Citi) reached an agreement concerning the auction rate securities purchased from Citi. The agreement provides that in June 2015, the State will have the option to require Citi to purchase some or all of the State's remaining auction rate securities portfolio at par as well as to have Citi make up the difference between liquidation price and par on any of the State's auction rate securities which have been previously involuntarily liquidated below par. The agreement also provides that starting July 2012, the State will have the ability to obtain interim liquidity on its auction rate securities portfolio of up to $150 million worth of securities, at market value, with the difference between that market value and par paid by Citi in July 2015.

Carrier Contracts

The carrier contracts for the active employees and retiree plans for the Trust Fund were extended from July 1, 2011 through December 27, 2011. Approvals were received from the State Procurement Office to extend these contracts.

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
STATE OF HAWAII

ENTERPRISE FUND

Schedule of Administrative Operating Expenses
(Supplementary Information)
Year ended June 30, 2010

		2010
Administrative operating expenses:		
Personnel services	$	1,668,784
Contracted services		1,787,862
Equipment		179,828
Occupancy		314,994
Printing and binding		75,278
Insurance		85,767
Repairs and maintenance		31,511
Postage		104,350
Telephone		24,858
Transportation		12,511
Rental of equipment		22,643
Supplies		21,340
Training		110
Other		5,075
Total administrative operating expenses	$	4,334,911