

**KENTUCKY ASSOCIATION OF COUNTIES
UNEMPLOYMENT COMPENSATION
SELF-INSURANCE FUND**

FINANCIAL STATEMENTS

Years Ended June 30, 2009 and 2008

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
Kentucky Association of Counties Unemployment
Compensation Self-Insurance Fund
Frankfort, Kentucky

We have audited the accompanying balance sheets of Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund as of June 30, 2009 and 2008, and the related statements of revenues, expenses and changes in members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund as of June 30, 2009 and 2008, and changes in members' equity and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Deming, Malone, Livesay & Ostroff

Louisville, Kentucky
April 12, 2010

**KENTUCKY ASSOCIATION OF COUNTIES
UNEMPLOYMENT COMPENSATION SELF-INSURANCE FUND**

BALANCE SHEETS
June 30, 2009 and 2008

	2009	2008
ASSETS		
Cash and cash equivalents	\$ 3,170,890	\$ 4,518,262
Investments, at fair market value	6,778,726	5,567,485
Premiums receivable, less allowance for doubtful accounts of \$15,000	1,277,117	884,939
Accrued interest receivable	38,662	31,067
Prepaid expenses	65,905	49,506
Total assets	\$ 11,331,300	\$ 11,051,259
LIABILITIES AND MEMBERS' EQUITY		
Unemployment compensation claims payable	\$ 450,045	\$ 396,201
Deferred revenue	1,299,655	1,046,597
Total liabilities	1,749,700	1,442,798
Members' equity	9,581,600	9,608,461
Total liabilities and members' equity	\$ 11,331,300	\$ 11,051,259

See Notes to Financial Statements.

**KENTUCKY ASSOCIATION OF COUNTIES
UNEMPLOYMENT COMPENSATION SELF-INSURANCE FUND**

**STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN MEMBERS' EQUITY**

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
REVENUES:		
Member premiums, net	\$ 2,350,864	\$ 2,054,293
Investment income	265,365	412,215
Realized gain (loss) on sale of investments	11,846	(6,890)
Unrealized loss on investments	<u>(96,855)</u>	<u>(48,508)</u>
Total revenues	<u>2,531,220</u>	<u>2,411,110</u>
EXPENSES:		
Unemployment compensation benefits	1,889,627	1,742,652
General and administrative expenses	517,454	470,241
KACO management fee	100,000	99,000
KACO royalty	1,000	1,000
Contribution to program guaranty fund	<u>50,000</u>	<u>50,000</u>
Total expenses	<u>2,558,081</u>	<u>2,362,893</u>
Excess of (expenses) revenues	(26,861)	48,217
Members' equity, beginning of year	<u>9,608,461</u>	<u>9,560,244</u>
Members' equity, end of year	<u><u>\$ 9,581,600</u></u>	<u><u>\$ 9,608,461</u></u>

See Notes to Financial Statements.

**KENTUCKY ASSOCIATION OF COUNTIES
UNEMPLOYMENT COMPENSATION SELF-INSURANCE FUND**

STATEMENTS OF CASH FLOWS
Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Cash received from member premiums	\$ 2,211,744	\$ 2,357,646
Investment income received	257,770	422,347
Unemployment compensation benefits paid	(1,835,783)	(2,036,459)
Cash paid to suppliers and others	<u>(634,853)</u>	<u>(545,647)</u>
Net cash (used in) provided by operating activities	<u>(1,122)</u>	<u>197,887</u>
Cash flows from investing activities:		
Contribution to program guaranty fund	(50,000)	(50,000)
Purchase of investments	(3,896,250)	(3,079,656)
Proceeds from sale and maturities of investments	<u>2,600,000</u>	<u>1,400,000</u>
Net cash used in investing activities	<u>(1,346,250)</u>	<u>(1,729,656)</u>
Net decrease in cash and cash equivalents	(1,347,372)	(1,531,769)
Cash and cash equivalents at beginning of year	<u>4,518,262</u>	<u>6,050,031</u>
Cash and cash equivalents at end of year	<u><u>\$ 3,170,890</u></u>	<u><u>\$ 4,518,262</u></u>

See Notes to Financial Statements.

	<u>2009</u>	<u>2008</u>
RECONCILIATION OF EXCESS OF (EXPENSES) REVENUES TO NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES		
Excess of (expenses) revenues	\$ (26,861)	\$ 48,217
Adjustments to reconcile excess of (expenses) revenues to net cash (used in) provided by operating activities:		
Realized (gain) loss on sale of investments	(11,846)	6,890
Unrealized loss on investments	96,855	48,508
Contribution to program guaranty fund	50,000	50,000
Changes in assets and liabilities:		
Decrease (increase) in:		
Premiums receivable	(392,178)	258,339
Accrued interest receivable	(7,595)	10,132
Prepaid expenses	(16,399)	24,594
Increase (decrease) in:		
Unemployment compensation claims payable	53,844	(293,807)
Deferred revenue	<u>253,058</u>	<u>45,014</u>
Total adjustments	<u>25,739</u>	<u>149,670</u>
Net cash (used in) provided by operating activities	<u>\$ (1,122)</u>	<u>\$ 197,887</u>

**KENTUCKY ASSOCIATION OF COUNTIES
UNEMPLOYMENT COMPENSATION SELF-INSURANCE FUND**

NOTES TO FINANCIAL STATEMENTS

Note 1. Description of Fund and Summary of Significant Accounting Policies

The Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund (Fund) was formed by the Kentucky Association of Counties (KACO) to receive contributions from eligible members to be used to reimburse the Commonwealth of Kentucky for unemployment compensation benefits paid to eligible members' employees. Governmental entities located in Kentucky who are members of KACO are eligible to make annual contributions to the Fund as determined by the Trustees in lieu of making contributions to the Kentucky Unemployment Compensation Fund. Each member is jointly and severally liable for reimbursing the Commonwealth in an amount equal to the quarterly benefits paid that are attributable to services performed in the employ of any or all members of the Fund.

Summary of significant accounting policies:

This summary of significant accounting policies of the Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund is presented to assist in the understanding of the Fund's financial statements. The financial statements and notes are representations of the Fund's management who is responsible for the integrity and objectivity of the financial statements. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.

Method of accounting:

The financial statements of the Fund have been prepared on the accrual basis of accounting.

Investments and credit risk:

Quoted market prices are used to value investments and are accounted for under Governmental Accounting Standards Board Statement (GASBS) No. 31 "Accounting and Financial Reporting for Certain Investments and for External Investment Pools".

NOTES TO FINANCIAL STATEMENTS

The Fund has significant investments in U.S. Treasury notes and mortgage-backed securities held by Central Bank & Trust Company and FSC Securities Corporation. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Because of the level of risk associated with certain investment securities, it is at least reasonably possible that changes in values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the balance sheet.

Premiums receivable:

Premiums receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to premiums receivable. Amounts are past due when not paid by the discount date.

Revenue recognition:

Member premiums revenue is recognized over the period to which the premiums relate. Premiums billed but not yet earned as of June 30, 2009 and 2008 are recorded as deferred revenue on the balance sheet.

Unemployment compensation claims payable:

The liability payable to the Commonwealth of Kentucky represents the actual benefits paid by the Commonwealth for the quarter ended June 30, 2009 and 2008.

Estimates:

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

NOTES TO FINANCIAL STATEMENTS

Cash and cash equivalents:

For purposes of the statement of cash flows, the Fund considers only cash and investments with an original maturity date of three months or less to be cash and cash equivalents.

Income taxes:

The Fund is exempt from income taxes under Section 115 of the Internal Revenue Code.

Legal, regulatory and geographic risk:

Legal and regulatory risk is the risk that changes in the legal or regulatory environment in which an insurer operates will occur and create additional losses or expenses not anticipated by the insurer in pricing its products. That is, regulatory initiatives designed to reduce insurer profits or new legal theories may create costs for the insurer beyond those currently recorded in the financial statements. The Fund is exposed to this risk, plus a geographic risk, by writing all of its business in Kentucky, thus increasing its exposure to a single jurisdiction.

Subsequent events:

Management has evaluated subsequent events through April 12, 2010, the date which the financial statements were available to be issued

NOTES TO FINANCIAL STATEMENTS

Note 2. Investments

Investments are carried at fair market value as determined based on quoted prices in active markets (all Level 1 measurements), Investments held in trust by Central Bank & Trust Company and FSC Securities Corporation at June 30, 2009 and 2008 consisted of the following:

	June 30, 2009		
	Face Value	Cost	Fair Market Value
U.S. Treasury notes	<u>\$ 815,000</u>	<u>\$ 817,613</u>	<u>\$ 825,954</u>
Mortgage-backed securities:			
Federal Home Loan Mortgage Corp.	2,200,000	2,200,005	2,197,364
Federal National Mortgage	<u>1,800,000</u>	<u>1,802,250</u>	<u>1,780,064</u>
	<u>4,000,000</u>	<u>4,002,255</u>	<u>3,977,428</u>
Eaton Vance Mutual Fund	<u>2,000,000</u>	<u>2,182,574</u>	<u>1,975,344</u>
Total investments	<u>\$6,815,000</u>	<u>\$7,002,442</u>	<u>\$6,778,726</u>
	June 30, 2008		
	Face Value	Cost	Fair Market Value
U.S. Treasury notes	<u>\$ 815,000</u>	<u>\$ 817,613</u>	<u>\$ 813,728</u>
Mortgage-backed securities:			
Federal Home Loan Mortgage Corp.	2,200,000	2,200,005	2,178,474
Federal National Mortgage	<u>600,000</u>	<u>588,154</u>	<u>605,436</u>
	<u>2,800,000</u>	<u>2,788,159</u>	<u>2,783,910</u>
Eaton Vance Mutual Fund	<u>2,000,000</u>	<u>2,088,574</u>	<u>1,969,847</u>
Total investments	<u>\$5,615,000</u>	<u>\$5,694,346</u>	<u>\$5,567,485</u>

NOTES TO FINANCIAL STATEMENTS

The aggregate fair market value of annual maturities of investments at June 30, 2009 and 2008, based upon stated maturity dates are as follows:

	<u>2009</u>	<u>2008</u>
Due one through five years	\$ 825,954	\$ 813,728
Eaton Vance Mutual Fund	1,975,344	1,969,847
Mortgage-backed securities	<u>3,977,428</u>	<u>2,783,910</u>
	<u>\$6,778,726</u>	<u>\$5,567,485</u>

Note 3. Members' Equity

Members' equity consists of separate accounts maintained for each member. Each member's equity balance is increased by its contributions and allocated share of investment and other revenues, and decreased by unemployment compensation benefits paid on its behalf, dividends distributed and allocated share of other expenses. At June 30, 2009 and 2008, members' equity consists of:

	<u>2009</u>	<u>2008</u>
Members with equity	\$10,608,692	\$10,829,992
Members with a deficit	<u>(1,027,092)</u>	<u>(1,221,531)</u>
Total members' equity	<u>\$ 9,581,600</u>	<u>\$ 9,608,461</u>

Note 4 Related Party Transactions

The Fund has a Program Administration Agreement whereby the Fund paid a set fee of \$127,825 and \$104,850 per quarter for 2009 and 2008, respectively, to KACO to provide management and administrative services for the Fund. The total fee is adjusted annually based upon the actual allocation of expenses covered by the agreement. For the years ended June 30, 2009 and 2008, actual expenses allocated to the Fund were \$51,631 and \$32,232 less than the program administration fee, respectively. This amount will be utilized to reduce the Fund's future payment to KACO and is included in prepaid expenses on the June 30, 2009 and 2008 balance sheets. An additional management fee of \$100,000 and \$99,000 was paid to KACO for the years ended June 30, 2009 and 2008, respectively.

NOTES TO FINANCIAL STATEMENTS

The Fund made a one-time contribution of \$30,000 to KACO for the renovation of KACO buildings. This amount is included in prepaid expenses on the June 30, 2009 and 2008 balance sheets and is being amortized over a ten year period that began January 1, 2003.

The Fund has a licensing agreement with KACO that requires the Fund to pay an annual royalty to KACO in return for the use of KACO's name and logo. The Fund paid royalties of \$1,000 and \$1,000 for the years ended June 30, 2009 and 2008.

The KACO Board of Trustees established a Program Guaranty Fund to provide additional financial protection for KACO sponsored entities in case an entity experiences financial difficulties. The Fund's contribution was \$50,000 for each of the years ended June 30, 2009 and 2008.

Note 5. Concentration of Credit Risk

The Fund maintains its cash accounts at various banks in Kentucky. Accounts at each bank are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. At June 30, 2009, the uninsured cash balances totaled approximately \$866,000.