

KACo Unemployment Compensation Self-Insurance Fund
Financial Statements
Years Ended June 30, 2021 and 2020

KACo Unemployment Compensation Self-Insurance Fund
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Years Ended June 30, 2021 and 2020

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Independent Auditor's Report

To the Board of Directors and Members of
KACo Unemployment Compensation Self-Insurance Fund

We have audited the accompanying financial statements of Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund (the "Fund"), which comprise the balance sheet as of June 30, 2021 and 2020, and the related statements of revenues, expenses and changes in members' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Independent Auditor's Report (Continued)

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of KACo Unemployment Compensation Self-Insurance Fund as of June 30, 2021 and 2020, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

MCM CPAs & Advisors LLP

Louisville, Kentucky
November 17, 2021

KACo Unemployment Compensation Self-Insurance Fund
Balance Sheets
June 30, 2021 and 2020

	<u>2021</u>	<u>2020</u>
Assets		
Cash and cash equivalents	\$ 3,532,154	\$ 2,083,700
Fixed maturity investments, at fair value	10,078,087	9,993,012
Equity securities, at fair value	2,520,233	2,133,766
Premiums receivable	711,165	1,005,615
Accrued interest receivable	41,262	54,851
Prepaid expenses	<u>46,162</u>	<u>72,256</u>
Total assets	<u>\$ 16,929,063</u>	<u>\$ 15,343,200</u>
Liabilities and members' equity		
Liabilities		
Accounts payable	\$ 8,814	\$ 8,135
Unemployment compensation benefits payable	54,014	-
Deferred revenue	<u>824,023</u>	<u>1,064,676</u>
Total liabilities	886,851	1,072,811
Members' equity	<u>16,042,212</u>	<u>14,270,389</u>
Total liabilities and members' equity	<u>\$ 16,929,063</u>	<u>\$ 15,343,200</u>

See accompanying notes.

KACo Unemployment Compensation Self-Insurance Fund
Statements of Revenues, Expenses and Changes in Members' Equity
Years Ended June 30, 2021 and 2020

	<u>2021</u>	<u>2020</u>
Revenues		
Members premiums, net	\$ 1,889,494	\$ 2,214,211
Investment income	291,242	352,250
Realized and unrealized gains on investments	<u>431,753</u>	<u>297,525</u>
Total revenues	2,612,489	2,863,986
Expenses		
Unemployment compensation benefits	247,120	1,027,070
General and administrative expenses	359,546	364,759
KACo management fee	233,000	225,000
KACo royalty	<u>1,000</u>	<u>1,000</u>
Total expenses	<u>840,666</u>	<u>1,617,829</u>
Excess of revenues over expenses	1,771,823	1,246,157
Members' equity, beginning of year	<u>14,270,389</u>	<u>13,024,232</u>
Members' equity, end of year	<u>\$ 16,042,212</u>	<u>\$ 14,270,389</u>

See accompanying notes.

KACo Unemployment Compensation Self-Insurance Fund
Statements of Cash Flows
Years Ended June 30, 2021 and 2020

	<u>2021</u>	<u>2020</u>
Cash flows from operating activities		
Cash received from member premiums	\$ 2,183,944	\$ 2,119,376
Investment income received, net of investment fees	291,242	344,020
Unemployment compensation benefits paid	(193,106)	(1,564,900)
Cash paid to suppliers and others	<u>(793,837)</u>	<u>(607,263)</u>
Net cash provided by operating activities	1,488,243	291,233
Cash flows from investing activities		
Purchase of investments	(6,932,184)	(2,478,104)
Proceeds from sales and maturities of investments	<u>6,892,395</u>	<u>2,461,433</u>
Net cash used in investing activities	<u>(39,789)</u>	<u>(16,671)</u>
Net increase in cash and cash equivalents	1,448,454	274,562
Cash, cash equivalents at beginning of year	<u>2,083,700</u>	<u>1,809,138</u>
Cash, cash equivalents at end of year	<u>\$ 3,532,154</u>	<u>\$ 2,083,700</u>

See accompanying notes.

KACo Unemployment Compensation Self-Insurance Fund
Statements of Cash Flows (Continued)
Years Ended June 30, 2021 and 2020

	<u>2021</u>	<u>2020</u>
Reconciliation of excess of revenues over expenses to net cash provided by operating activities		
Excess of revenues over expenses	\$ 1,771,823	\$ 1,246,157
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities		
Realized gains on investments	(279,393)	(93,466)
Unrealized gain on investments	(152,360)	(204,059)
Changes in assets and liabilities		
Decrease (increase) in		
Premiums receivable	294,450	(12,169)
Accrued interest receivable	13,589	(2,075)
Prepaid expenses	26,094	(22,883)
Increase (decrease) in		
Accounts payable	679	224
Unemployment compensation benefits payable	54,014	(537,830)
Deferred revenue	<u>(240,653)</u>	<u>(82,666)</u>
Total adjustments	<u>(283,580)</u>	<u>(954,924)</u>
Net cash provided by operating activities	<u>\$ 1,488,243</u>	<u>\$ 291,233</u>

See accompanying notes.

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements
Years Ended June 30, 2021 and 2020

Note A - Nature of Operations

The Kentucky Association of Counties Unemployment Compensation Self-Insurance Fund ("Fund") was organized as a nonprofit fund by the Kentucky Association of Counties ("KACo"). The Fund was established as a service to KACo members and their related agencies who elect coverage ("Members") under the Kentucky Unemployment Compensation Amendments of 1976 and KRS 341.277. These statutes provide that governmental entities, in lieu of making contributions to the Kentucky Unemployment Compensation Fund, can elect to reimburse the Commonwealth of Kentucky (the "Commonwealth") for all benefits paid to workers for compensable weeks of unemployment. 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.

The Members pay annual premiums to the Fund based upon premium rates determined by an actuary and approved by the Board of Trustees. Benefits paid by the Commonwealth are reimbursed by the Fund and charged to each member's account. The Bylaws provide that each member is responsible for all benefits paid to its employees, and each can be required to make additional premium payments to the Fund if a member has a deficient equity balance. Thus, the Fund assumes no liability for member deficit balances, as it operates as a pool of self-insured members rather than as a group self-insurer. As of June 30, 2021 and 2020, participation in the Fund included 477 members.

Note B - Summary of Significant Accounting Policies

1. Basis of Presentation: The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The Accounting Standards Codification ("ASC") as produced by the Financial Accounting Standards Board ("FASB") is the sole source of authoritative accounting technical literature.
2. Use of Estimates: Management uses estimates and assumptions in preparing these financial statements in accordance with GAAP. Those estimates and assumptions affect the reported amounts of assets and liabilities, 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. Premium Receivables: Members premium revenues are billed on a calendar year basis. A discount is applied to premiums paid timely based on management's discretion. The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible uncollectible accounts based on prior experience. Amounts are charged against the allowance when management determines that collectability is doubtful. There was not an allowance recorded at June 30, 2021 and 2020.
4. Cash and Cash Equivalents: The Fund considers all highly liquid investments with a maturity when purchased of three months or less not restricted for a specific purpose, to be cash equivalents. The Fund typically maintains balances with its bank in excess of federally insured limits.
5. Marketable Securities: Investments are recorded at fair value. Net realized and unrealized gains and losses are recognized in the statement of revenues, expenses and changes in members' equity.

The Fund has significant investments in U.S. governmental agency and mortgage-backed securities, corporate bonds and notes, and equity securities. 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. The Fund considers all investments to be classified as available-for-sale. Cost basis is determined on historical purchase price (see Notes D and E).

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements (Continued)
Years Ended June 30, 2021 and 2020

Note B - Summary of Significant Accounting Policies (Continued)

6. Unemployment Compensation Benefits Payable: The liability payable to the Commonwealth of Kentucky represents the actual benefits paid by the Commonwealth for the quarters ended June 30, 2021 and 2020. The liability for unemployment benefits payable to the Commonwealth represents quarterly benefits paid by the Commonwealth during the year that were reimbursed by the Fund subsequent to year end. The Fund does not recognize any liability for future benefits that may become payable relating to unemployment prior to year-end since each member is ultimately liable for benefits paid to its employees. See Note H for additional information.
7. Premium Revenue: Members premium revenues are recognized on a pro-rata basis over the coverage period, which is typically the calendar year. Premiums billed related to the unexpired portion of policies in force at the balance sheet date are recorded as deferred revenue on the balance sheets.
8. Income Taxes: The fund is exempt from income taxes under section 115 of the Internal Revenue Code, which pertains to instrumentalities of state and governments. However, income from certain activities not directly related to the Fund's tax-exempt purpose may be subject to taxation as unrelated business income.

As of June 30, 2021, and 2020, the fund did not have any accrued interest or penalties related to income tax liabilities, and no interest or penalties have been charged to operations for the years then ended.

9. Fair Value Measurements: The Fund applies GAAP for fair value measurements of financial assets that are recognized or disclosed at fair value in the financial statements on a recurring basis. GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP also establishes a framework for measuring fair value and expands disclosures about fair value measurements. See Note E.
10. Recent Accounting Pronouncements: In June 2016, the FASB issued Accounting Standards Update No. 2016-13 ("ASU 2016-13"), Financial Instruments - Credit Losses (Topic 326). The standard requires a financial asset (including premium receivables) measured at amortized cost basis to be presented at the net amount expected to be collected. Thus, the statement of income will reflect the measurement of credit losses for newly recognized financial assets as well as the expected increases or decreases of expected credit losses that have taken place during the period. This standard will be effective for the year ending June 30, 2024. The Fund is currently in the process of evaluating the impact of adoption of this ASU on the financial statements.
11. Subsequent Events: Subsequent events for the Company have been considered through the date of the Independent Auditor's Report which represents the date the financial statements were available to be issued (see Note I).

Note C - Cash and Equivalents

Cash and equivalents at June 30, 2021 and 2020 are comprised of the following:

	<u>2021</u>	<u>2020</u>
Checking account	\$ 2,747,832	\$ 1,553,223
Money market funds	<u>784,322</u>	<u>530,477</u>
	<u>\$ 3,532,154</u>	<u>\$ 2,083,700</u>

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements (Continued)
Years Ended June 30, 2021 and 2020

Note D - Investments

Investments held in trust by Central Bank & Trust Company at June 30, 2021 and 2020 consisted of the following:

	<u>2021</u>	<u>2020</u>
U.S. governmental agency and mortgage-backed securities		
Federal national mortgage	\$ 5,055,320	\$ 2,838,054
U.S. treasury notes	2,460,093	4,380,957
Federal Home Loan Mortgage Gold Pool	<u>13,542</u>	<u>19,267</u>
	7,528,955	7,238,278
Corporate bonds and notes	2,299,132	2,504,734
Municipal bonds	250,000	250,000
Common stocks	<u>2,520,233</u>	<u>2,133,766</u>
 Total investments	 <u>\$ 12,598,320</u>	 <u>\$ 12,126,778</u>

The aggregate fair value of annual maturities of U.S. governmental agency and mortgage-backed securities, municipal and corporate bonds and notes at June 30, 2021, based on stated maturity dates are as follows:

	<u>Cost</u>	<u>Fair value</u>
Due in one year or less	\$ 773,834	\$ 783,005
Due after one year through five years	3,262,280	3,468,700
Due after five years through ten years	1,676,095	1,754,913
Due after ten years	<u>4,039,491</u>	<u>4,071,469</u>
	<u>\$ 9,751,700</u>	<u>\$ 10,078,087</u>

Investment income consisted of the following:

	<u>2021</u>	<u>2020</u>
Interest and other investment income	\$ 291,242	\$ 352,250
Net gain on sale of investments	279,393	93,466
Change in unrealized gains on investments	<u>152,360</u>	<u>204,059</u>
	722,995	649,775
Less: investment management fees	<u>(40,650)</u>	<u>(38,010)</u>
	<u>\$ 682,345</u>	<u>\$ 611,765</u>

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements (Continued)
Years Ended June 30, 2021 and 2020

Note E - Fair Value Measurements

The Fund applies GAAP for fair value measurements of financial assets that are recognized or disclosed at fair value in the financial statements on a recurring basis. GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements).

The three levels of the fair value hierarchy are as follows:

- Level 1: inputs are quoted prices (unadjusted) in active markets for identical assets that the Company has the ability to access at the measurement date.
- Level 2: inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: inputs are unobservable inputs for the asset or liability.

Following is a description of the valuation methodologies for assets measured at fair value. There have been no changes in methodologies used at June 30, 2021 and 2020.

The Fund's Level 1 investments include equity securities that are traded in an active exchange market, as well as one U.S. Treasury securities whose value is set by government statute.

The Funds' Level 2 investments include fixed maturities with quoted prices that are traded less frequently than exchange-traded instruments or instruments whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes fixed maturities where fair values are obtained from a nationally recognized, third-party pricing service.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Fund believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following is a summary of the Fund's financial assets that are accounted for at fair value on a recurring basis by level in accordance with the fair value hierarchy described above:

	Investments at fair value as of June 30, 2021			
	Level 1	Level 2	Level 3	Total
Common stock	\$ 2,520,233	\$ -	\$ -	\$ 2,520,233
U.S treasury notes	5,068,862	-	-	5,068,862
Government bonds	-	2,460,093	-	2,460,093
Corporate and municipal bonds	-	2,549,132	-	2,549,132
Total	<u>\$ 7,589,095</u>	<u>\$ 5,009,225</u>	<u>\$ -</u>	<u>\$ 12,598,320</u>

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements (Continued)
Years Ended June 30, 2021 and 2020

Note E - Fair Value Measurements (Continued)

	Investments at fair value as of June 30, 2020			Total
	Level 1	Level 2	Level 3	
Common stock	\$ 2,133,766	\$ -	\$ -	\$ 2,133,766
U.S treasury notes	4,380,957	-	-	4,380,957
Government bonds	-	2,857,321	-	2,857,321
Corporate and municipal bonds	-	2,754,734	-	2,754,734
Total	<u>\$ 6,514,723</u>	<u>\$ 5,612,055</u>	<u>\$ -</u>	<u>\$ 12,126,778</u>

Investments are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices of like or similar securities, if available and these securities are classified as Level 1 or Level 2. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions and are classified as Level 3.

There were no transfers between Levels 1, 2 and 3 for the years ended June 30, 2021 and 2020.

Note F - Members' Equity

Member's equity consists of separate accounts maintained for each member. Each member's equity balance is increased by its contributions and allocated share of investment income and other revenues, decreased by unemployment compensation benefits paid on its behalf, dividends distributed and the allocated share of other expenses. There were no dividends paid to members or assessments charged during the years ended June 30, 2021 and 2020. At June 30, 2021 and 2020, members' equity consisted of the following:

	2021	2020
Members with equity	\$ 16,578,067	\$ 15,015,232
Members with a deficit	(535,855)	(744,843)
	<u>\$ 16,042,212</u>	<u>\$ 14,270,389</u>

Note G - Related Party Transactions

The Fund has a Program Administration Agreement whereby the Fund paid a set fee of \$81,625 and \$81,738 per quarter for the years ended June 30, 2021 and 2020, 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, 2021 and 2020, expenses for the Fund were \$280,338 and \$254,696, respectively. The excess payments of \$46,162 and \$72,256 for the years ended June 30, 2021 and 2020, respectively, are utilized to reduce the Fund's future payments to KACo and is included in prepaid expenses on June 30, 2021 and 2020 balance sheets. An additional management fee of \$233,000 and \$225,000 was paid to KACo for the years ended June 30, 2021 and 2020, respectively.

KACo Unemployment Compensation Self-Insurance Fund
Notes to Financial Statements (Continued)
Years Ended June 30, 2021 and 2020

Note G - Related Party Transactions (Continued)

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 for each of the years ended June 30, 2021 and 2020.

Included in fixed maturity investments is a KACo bond with a carrying amount of \$250,000 as of June 30, 2021 and 2020. The KACo bond accrues interest at 1.57% per annum and matures at February 1, 2040.

Note H - COVID-19

In March 2020, the World Health Organization declared the global novel coronavirus disease 2019 ("COVID-19") outbreak a pandemic. Additionally, the United States Centers for Disease Control and Prevention confirmed the spread of the disease throughout the United States. As of the date the accompanying financial statements were available to be issued, the Fund's operations have not been adversely impacted as a result of COVID-19, however the full impact on the Fund is generally not known at this point as the scale and severity of the outbreak, and the resulting short-term and long-term economic impact, is still largely unknown.

In response to the expected increase in unemployment claims due to the pandemic, the U.S. federal government initially notified states that federal funding would be provided to reimburse the states to provide relief to employers, including the Fund, that reimburse the state for unemployment insurance claims paid on their behalf. The Fund was initially only required to reimburse 50% of the unemployment compensation benefits to the state that would typically be paid in full by the Fund. In December 2020, the Office of the Governor of the Commonwealth of Kentucky and the Office of Unemployment Insurance notified the Fund and all reimbursing employers that federal CARES Act funds would be applied to the state Unemployment Insurance Trust Fund to cover the remaining 50% of unemployment compensation benefits owed by the Fund and other reimbursing employers for the period from April 1, 2020 through December 31, 2020. Therefore, the Fund does not expect to owe any unemployment compensation benefits reimbursement for the quarters ended June 30, 2020, September 30, 2020 or December 31, 2020 and has not recorded any unemployment compensation benefits expense for these periods.

Additionally, in March 2021 the American Rescue Plan Act of 2021 was enacted by the federal government and provides 75% relief for reimbursing employer benefit charges accrued during the period April 4, 2021 through September 4, 2021. As a result of the state and federal relief funds committed by the legislation and state orders above, The Fund was responsible to reimburse for only 50% and 25%, respectively, of unemployment compensation benefits for the quarters ended March 31, 2021 and June 30, 2021. In the event the Governor or federal government were to revise this guidance, the ultimate outcome of the liability could still be subject to change; however, the Fund's management believes the likelihood of a material change to this claims liability is remote.

Note I - Subsequent Event

Subsequent to year end, in July 2021, the Fund's Board of Trustees approved a return of prior year's premium contributions to all eligible members. The return of contribution payments totaled \$2,295,389 and were disbursed in August 2021. The amount of the return of contribution payments was determined by the member premiums paid into the Fund related to calendar year 2019.