

**Kentucky Associated General
Contractors Self Insurers' Fund**

Financial Statements

Years Ended December 31, 2019 and 2018

Kentucky Associated General Contractors Self Insurers' Fund
Table of Contents
Years Ended December 31, 2019 and 2018

	<u>Page</u>
Independent Auditor's Report	1 - 2
Financial Statements	
Balance Sheets	3
Statements of Operations and Comprehensive Income (Loss)	4
Statements of Changes in Fund Balance.....	5
Statements of Cash Flows.....	6
Notes to Financial Statements.....	7 - 16
Required Supplementary Information.....	17 - 18



Independent Auditor's Report

To the Board of Trustees
Kentucky Associated General Contractors Self Insurers' Fund

Report on the Financial Statements

We have audited the accompanying financial statements of the Kentucky Associated General Contractors Self Insurers' Fund (the "Fund"), which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of operations and comprehensive income (loss), changes in fund balance, 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 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 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 the Kentucky Associated General Contractors Self Insurers' Fund as of December 31, 2019 and 2018, 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.

Change in Accounting Principle

As discussed in Note B to the financial statements, the Fund has changed its method of accounting for certain equity investments by recognizing the change in fair value in net income effective January 1, 2019 due to the adoption of Accounting Standards Update 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*.

Uncertainties Regarding the Liability for Estimated Claims

As discussed in Note B in the accompanying financial statements, the estimated liability for claims reflected in the accompanying financial statements is based upon an evaluation by an independent actuary. Although management believes that this estimate is reasonable, because of inherent uncertainties in estimating this liability, it is reasonably possible that changes in such estimates may occur and can be material in relation to the financial statements as a whole. Our opinion is not modified with respect to that matter.

Report on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the cumulative incurred losses and loss-adjustment expenses, cumulative paid losses and loss-adjustment expenses, and average annual percentage payout of incurred claims information for the years through 2019 be presented to supplement the basic financial statements (the "required supplementary information"). Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information prior to 2017 because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance on the information prior to 2017.

MCM CPAs & Advisors LLP

Louisville, Kentucky
April 10, 2020

Kentucky Associated General Contractors Self Insurers' Fund
Balance Sheets
December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Assets		
Cash and cash equivalents	\$ 22,552,631	\$ 23,215,052
Investments		
Fixed maturities available-for-sale, at fair value	275,533,913	265,240,231
Equity securities, at fair value	<u>115,974,220</u>	<u>90,091,088</u>
Total investments	391,508,133	355,331,319
Premiums	8,013,140	8,927,147
Aggregate excess insurance	473,901	449,417
Specific excess insurance	34,691,954	24,189,488
Accrued interest	1,512,550	1,483,840
Income taxes receivable	11,471,412	4,715,172
Prepaid reinsurance	<u>1,345,602</u>	<u>1,218,202</u>
Total assets	<u>\$ 471,569,323</u>	<u>\$ 419,529,637</u>
Liabilities and fund balance		
Liabilities		
Estimated liability for claims		
Incurred and reported	\$ 139,432,862	\$ 131,287,471
Incurred but not reported and loss adjustment expense	137,536,954	146,402,853
Unallocated loss-adjustment expense	<u>4,225,831</u>	<u>4,225,831</u>
Total estimated liability for claims	281,195,647	281,916,155
Premiums refundable	1,387,991	1,398,344
Service fee and other fees payable	4,248,721	4,544,664
Member deposits	9,489,835	9,911,853
Tax assessments collected on premiums	932,173	976,727
Deferred tax liability	11,620,579	6,725,835
Accrued member dividends	<u>69,643,396</u>	<u>44,692,170</u>
Total liabilities	<u>378,518,342</u>	<u>350,165,748</u>
Fund balance		
Retained earnings	92,333,822	41,161,646
Accumulated other comprehensive income, net of income taxes	<u>717,159</u>	<u>28,202,243</u>
Total fund balance	<u>93,050,981</u>	<u>69,363,889</u>
Total liabilities and fund balance	<u>\$ 471,569,323</u>	<u>\$ 419,529,637</u>

See accompanying notes.

**Kentucky Associated General Contractors Self Insurers' Fund
Statements of Operations and Comprehensive Income (Loss)
Years Ended December 31, 2019 and 2018**

	<u>2019</u>	<u>2018</u>
Revenues		
Premiums earned	\$ 56,980,247	\$ 60,972,870
Net investment income	8,958,778	8,302,070
Net realized investment gains	1,728,524	970,146
Unrealized gains on equity securities	22,958,104	-
Other	<u>240,943</u>	<u>365,768</u>
Total revenues	90,866,596	70,610,854
Expenses		
Claims incurred	20,460,196	45,256,380
Service fee	8,996,301	8,327,035
Commissions	5,676,132	6,078,128
Excess insurance premiums	1,644,996	1,445,003
Loss control	742,324	776,177
Premium audits	490,000	500,000
Other operating expenses	<u>2,276,887</u>	<u>2,217,556</u>
Total expenses	40,286,836	64,600,279
Income before dividends declared to members and income tax benefit	50,579,760	6,010,575
Dividends declared to members	<u>33,000,000</u>	<u>11,000,000</u>
Income (loss) before income tax benefit	17,579,760	(4,989,425)
Income tax benefit	<u>(2,753,122)</u>	<u>(1,208,092)</u>
Net income (loss)	20,332,882	(3,781,333)
Other comprehensive income (loss) - before tax		
Unrealized gains (losses) on investments		
Unrealized holding gains (losses) arising during the year	4,294,692	(6,401,528)
Reclassification adjustments for gains included in net income (loss)	<u>(48,857)</u>	<u>(970,146)</u>
Other comprehensive income (loss) before tax	4,245,835	(7,371,674)
Income tax (expense) benefit relative to other comprehensive income (loss), net	<u>(891,625)</u>	<u>1,548,052</u>
Other comprehensive income (loss), net of tax	<u>3,354,210</u>	<u>(5,823,622)</u>
Comprehensive income (loss)	<u>\$ 23,687,092</u>	<u>\$ (9,604,955)</u>

See accompanying notes.

Kentucky Associated General Contractors Self Insurers' Fund
Statements of Changes in Fund Balance
Years Ended December 31, 2019 and 2018

	Retained earnings	Accumulated other comprehensive income, net	Fund balance
	<u> </u>	<u> </u>	<u> </u>
Balance at December 31, 2017	\$ 50,542,156	\$ 28,426,688	\$ 78,968,844
Net loss	(3,781,333)	-	(3,781,333)
Reclassification of stranded tax effects from rate reduction	(5,599,177)	5,599,177	-
Other comprehensive loss, net tax	-	(5,823,622)	(5,823,622)
	<u> </u>	<u> </u>	<u> </u>
Balance at December 31, 2018	41,161,646	28,202,243	69,363,889
Net income	20,332,882	-	20,332,882
Cumulative impact of adoption of ASU 2016-01 as of January 1, 2019 (Note B)	30,839,294	(30,839,294)	-
Other comprehensive income, net tax	-	3,354,210	3,354,210
	<u> </u>	<u> </u>	<u> </u>
Balance at December 31, 2019	<u><u>\$ 92,333,822</u></u>	<u><u>\$ 717,159</u></u>	<u><u>\$ 93,050,981</u></u>

See accompanying notes.

Kentucky Associated General Contractors Self Insurers' Fund
Statements of Cash Flows
Years Ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Cash flows from operating activities		
Net income (loss)	\$ 20,332,882	\$ (3,781,333)
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Dividends declared to members	33,000,000	11,000,000
Change in unrealized gains on equity securities	(22,958,104)	-
Gain on sale of investments	(1,728,524)	(970,146)
Deferred income taxes	4,003,119	(9,825,831)
Amortization of investment premiums and discounts, net	(121,134)	521,152
Changes in assets and liabilities		
Receivables	(9,641,653)	604,157
Prepaid insurance	(127,400)	45,798
Income taxes receivable	(6,756,240)	8,684,399
Estimated liability for claims	(720,508)	14,170,297
Payables and accrued expenses	(306,296)	(396,931)
Member deposits	(422,018)	(146,478)
Tax assessments collected on premiums	(44,554)	(22,562)
	<u>14,509,570</u>	<u>19,882,522</u>
Cash flows from investing activities		
Purchases of investments	(182,870,137)	(60,539,033)
Proceeds from maturities and sales of investments	<u>175,746,920</u>	<u>52,973,384</u>
	<u>(7,123,217)</u>	<u>(7,565,649)</u>
Cash flows from financing activities		
Payment of dividends to members	<u>(8,048,774)</u>	<u>(13,377,859)</u>
	(662,421)	(1,060,986)
Cash and cash equivalents - beginning of year	<u>23,215,052</u>	<u>24,276,038</u>
Cash and cash equivalents - end of year	<u><u>\$ 22,552,631</u></u>	<u><u>\$ 23,215,052</u></u>

See accompanying notes.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements
Years Ended December 31, 2019 and 2018

Note A - Nature of Organization and Operations

The purpose of the Kentucky Associated General Contractors Self Insurers' Fund is to meet and fulfill employer member obligations and liabilities under the Kentucky Workers' Compensation Act, pursuant to KRS Section 342.350. The operations of the Fund are covered under a Trust Agreement. Insurance coverage is provided to members of construction industry associations in Kentucky. Claims administration and management services are provided by Ladegast & Heffner Claims Service, Inc. under a contract that extends through December 31, 2024. The service fee is based on a percentage of premiums earned.

Note B - Significant Accounting Policies

1. Basis of Accounting: 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 GAAP.
2. Use of Estimates: The preparation of financial statements in conformity with GAAP 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 the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant of these estimates is the estimated liability for claims, including the estimated liability for incurred but not reported claims. The Fund continually updates its estimates as additional data becomes available and adjusts the financial statements as deemed necessary. Although recorded reserves for losses and loss adjustment expenses are supported by actuarial computations, and other supportive data, the estimates are ultimately based on management's expectations of future events. Other estimates such as investment valuation, the collectability of reinsurance balances, and recoverability of deferred tax assets are regularly monitored, evaluated and adjusted.

3. Cash and Cash Equivalents: Cash equivalents include money market funds and certain investments with maturities of three months or less when purchased, cash and cash equivalents stated at cost, which approximates fair value. The Fund's bank balances are held at a single financial institution, and at times, balances may exceed federally insured amounts.
4. Investments: Effective January 1, 2019, the Company adopted Accounting Standards Update (ASU) 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. As such, equity securities which primarily include common stocks and mutual funds are now carried at fair value with the periodic change in fair value recognized in net income in the accompanying statements of operations and comprehensive income (loss). The associated deferred tax expense on the periodic change in fair value recognized is included in the provision for income taxes. Prior to 2019, marketable securities not classified as either trading or held-to-maturity were reported at fair value, adjusted for other-than-temporary declines in fair value, with unrealized gains and losses reported as a separate component of fund balance, net of any deferred taxes.

Realized gains and losses are determined on the specific identification method. In evaluating potential impairment, management considers, among other criteria: the current fair value compared to amortized cost or cost, as appropriate; the length of time the security's fair value has been below amortized cost or cost; management's intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in value; specific credit issues related to the issuer; and current economic conditions. Other-than-temporary impairment losses result in a permanent reduction of the cost basis of the underlying investment. During 2019 and 2018, the Fund did not record any other-than-temporary impairments.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note B - Significant Accounting Policies (Continued)

4. Investments (Continued): The fair value of a financial instrument is the amount 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 (the exit price). Observable inputs or unobservable inputs, defined by the FASB ASC Topic 820, *Fair Value Measurements*, may be used in the calculation of fair value. ASC Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value.

The three levels of the fair value hierarchy are described below:

- Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2: Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly. Level 2 securities are valued using third-party pricing services. These services may use, for example, model-based pricing models that utilize observable market data as inputs. Broker-dealer bids or quotes of securities with similar characteristics may also be used. There were no transfers between Level 1 and Level 2 securities in the current year;
- Level 3: Prices or valuations that require inputs that are both significant to the fair value measure and unobservable.

In accordance with ASC Topic 820, assets measured at fair value on a recurring basis are as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
December 31, 2019				
Investment securities				
U.S. Treasury notes and bonds	\$ -	\$ 142,569,554	\$ -	\$ 142,569,554
Domestic common stocks				
Technology common stocks	25,243,387	-	-	25,243,387
Basic material common stocks	7,512,252	-	-	7,512,252
Financial common stocks	13,072,017	-	-	13,072,017
Healthcare common stocks	10,490,795	-	-	10,490,795
Other common stocks and mutual funds	59,655,769	-	-	59,655,769
Corporate obligations	-	33,233,579	-	33,233,579
Municipal obligations	-	99,730,780	-	99,730,780
	<u>\$ 115,974,220</u>	<u>\$ 275,533,913</u>	<u>\$ -</u>	<u>\$ 391,508,133</u>
Total				

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note B - Significant Accounting Policies (Continued)

4. Investments (Continued):

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
December 31, 2018				
Investment securities				
U.S. Treasury notes and bonds	\$ -	\$ 147,754,966	\$ -	\$ 147,754,966
Domestic common stocks				
Technology common stocks	15,856,835	-	-	15,856,835
Basic material common stocks	6,170,456	-	-	6,170,456
Financial common stocks	8,972,821	-	-	8,972,821
Healthcare common stocks	16,381,653	-	-	16,381,653
Other common stocks and mutual funds	42,709,323	-	-	42,709,323
Corporate obligations	-	30,296,335	-	30,296,335
Municipal obligations	-	87,188,930	-	87,188,930
	<u>\$ 90,091,088</u>	<u>\$ 265,240,231</u>	<u>\$ -</u>	<u>\$ 355,331,319</u>
Total				

The Fund does not value any liabilities at fair value. The Fund does not measure any assets or liabilities at fair value on a nonrecurring basis. For all other classes of financial instruments, the carrying amount approximates fair value due to the short-term nature of the asset or liability. Investments, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. It is reasonably possible that changes in the investment values could occur in the near term and that such changes could materially affect the amounts reported in the balance sheets.

5. Estimated Liability for Claims: Estimates of the liability for incurred (reported and not reported) claims are actuarially determined using development factor methods. These methods use past observed patterns of the time between when a claim is incurred and when a claim is paid to estimate ultimate incurred claims from available paid claims information. Liabilities are based on the estimated ultimate cost of settling the claims. The unpaid claims liabilities are necessarily based on estimates and, accordingly, the ultimate liability may be in excess of or less than the amounts provided. Adjustments to the estimated liability for claims are charged or credited to expense in the periods in which they become known. Any adjustments could be material to the financial statements. In accordance with ASC Topic 210, *Balance Sheet - Offsetting*, estimated amounts of excess insurance recoverable are shown as assets, and are not netted against the estimated liability for claims as of December 31, 2019 and 2018. The estimated liability for claims is discounted using an interest rate of 1.8% on December 31, 2019 (compared to 2.5% as of December 31, 2018).
6. Member Dividends: Distributions to members in the form of dividends may be declared by the Board of Trustees, but under Kentucky Department of Insurance Regulations, dividends may not be paid until the end of the thirty-sixth month after the expiration of the self-insurance term. All insurance coverage is written under short duration, participating insurance contracts with a calendar year end expiration. The Fund reflects dividends as a charge to income and a liability in the year declared.
7. Premiums Earned: The Fund enters into individual workers' compensation insurance policy contracts with each Member Company, thus forming a group self-insured fund. Premiums are generally due at the beginning of each month based on the previous month's payroll exposure plus any current period known charges. Premiums are recognized as revenue during the period in which the Fund is obligated to provide coverage to said group of employers.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note B - Significant Accounting Policies (Continued)

8. Member Deposits: Member deposits represent 25% of each member's estimated normal premium at the inception of membership in the Fund. Member deposits are subject to periodic updates based on each member's most recent audited payroll and the resulting premium. Once a member's coverage through the Fund has been terminated and all outstanding balances due to the Fund have been paid, the member's deposit will be refunded.
9. Comprehensive Income (Loss): Comprehensive income (loss) includes all changes in equity during a period except those resulting from investments by members and distributions to members. Other comprehensive income (loss) is reported net of realized capital gains and losses and taxes.
10. Subsequent Events: Subsequent events for the Fund 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).
11. Recent Accounting Pronouncements: In May 2014, the FASB updated its guidance related to the Revenue from Contracts with Customers Topic 606 of the ASC. The objective of this update (and other related following updates) is to improve the reporting of revenue by providing a more robust framework for addressing revenue issues, and improved disclosure requirements. Current revenue recognition guidance in U.S. GAAP is comprised of broad revenue recognition concepts together with numerous revenue requirements for particular industries or transactions, which sometimes result in different accounting for economically similar transactions. For the Fund, this guidance is to be applied retrospectively to annual and interim reporting periods beginning after December 15, 2018. The Fund has adopted this guidance as of January 1, 2019. Since premium revenue from insurance contracts is excluded, the Fund has only minimal revenue items that are covered by this guidance. Adoption of this guidance had no impact on the financial condition or operating results of the Fund.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments-Credit Losses*. The standard requires a financial asset (including trade receivables) measured at amortized cost basis to be presented at the net amount expected to be collected. Thus, the income statement 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 calendar year ending December 31, 2023. The Fund intends to adopt this guidance upon the effective date listed and is currently evaluating the related impact on the financial statements.

In February 2018, the FASB issued ASU 2018-02, *Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. This guidance allows a reclassification between accumulated other comprehensive income and retained earnings for stranded tax effects associated with the change in the federal corporate income tax rate due to the passing of the Tax Cuts and Jobs Act (Tax Act) on December 22, 2017. An entity that elects to reclassify these amounts must reclassify the stranded tax effects related to the change in the federal corporate income tax rate for all items accounted for in other comprehensive income (loss). This guidance was effective for all entities for fiscal years beginning after December 15, 2018. The Fund has elected to adopt the guidance under ASU 2018-02 effective January 1, 2018 and the amount of stranded tax effect related to unrealized gains in accumulated other comprehensive income at December 31, 2017 is \$5,599,177. The adjustment was recorded as a reclassification to accumulated other comprehensive income from retained earnings as of January 1, 2018.

12. Reclassifications: Certain reclassifications were made to the 2018 financial statements to conform to the 2019 presentation. There was no impact on the fund balance or net income as a result of the changes.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note C - Investments

Investments at December 31, 2019 and 2018 include the following:

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
December 31, 2019				
U.S. Treasury notes and bonds	\$ 141,848,342	\$ 795,106	\$ (73,894)	\$ 142,569,554
Domestic common stock				
Technology common stocks	9,441,820	15,801,567	-	25,243,387
Basic material common stocks	5,989,273	1,801,718	(278,739)	7,512,252
Financial common stocks	6,369,864	6,702,153	-	13,072,017
Healthcare common stocks	4,432,728	6,058,067	-	10,490,795
Other common stocks and mutual funds	27,745,350	33,211,734	(1,301,315)	59,655,769
Corporate obligations	32,786,154	452,286	(4,861)	33,233,579
Municipal obligations	99,969,112	93,090	(331,422)	99,730,780
	<u>\$ 328,582,643</u>	<u>\$ 64,915,721</u>	<u>\$ (1,990,231)</u>	<u>\$ 391,508,133</u>
December 31, 2018				
U.S. Treasury notes and bonds	\$ 148,514,193	\$ 637,885	\$ (1,397,112)	\$ 147,754,966
Domestic common stock				
Technology common stocks	6,838,177	9,018,658	-	15,856,835
Basic material common stocks	5,050,430	1,300,258	(180,232)	6,170,456
Financial common stocks	5,551,663	3,421,158	-	8,972,821
Healthcare common stocks	9,109,328	7,272,325	-	16,381,653
Other common stocks and mutual funds	24,504,409	19,876,413	(1,671,499)	42,709,323
Corporate obligations	30,601,215	29,228	(334,108)	30,296,335
Municipal obligations	89,462,863	84,005	(2,357,938)	87,188,930
	<u>\$ 319,632,278</u>	<u>\$ 41,639,930</u>	<u>\$ (5,940,889)</u>	<u>\$ 355,331,319</u>

The components of net investment income as of December 31, 2019 and 2018, are presented below:

	2019	2018
Investment income		
Interest on fixed income securities	\$ 6,971,751	\$ 6,640,684
Dividends on equity securities	2,399,554	2,127,541
Other investment income	215,928	132,021
Less investment expenses	<u>(628,455)</u>	<u>(598,176)</u>
Net investment income	<u>\$ 8,958,778</u>	<u>\$ 8,302,070</u>

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note C - Investments (Continued)

The components of net realized investment gains (losses) and equity valuation increases included in earnings for the years ended December 31, 2019 and 2018, are as follows:

	<u>2019</u>	<u>2018</u>
Net realized investment gains (losses) and equity valuation increases		
Fixed income		
Gross realized gains	\$ 52,716	\$ 17,719
Gross realized losses	<u>(3,859)</u>	<u>(157,490)</u>
Net fixed income investment gains (losses)	48,857	(139,771)
Equity securities		
Gross unrealized gains and losses recorded during the year on equity securities still held at December 31, 2019	22,958,104	-
Gross realized gains	1,679,667	2,308,430
Gross realized losses	<u>-</u>	<u>(1,198,513)</u>
Net equity investment gains	<u>24,637,771</u>	<u>1,109,917</u>
Net realized investment gains and equity valuation increases	<u>\$ 24,686,628</u>	<u>\$ 970,146</u>

Debt securities held as of December 31, 2019 have contracted maturities as follows:

	<u>Amortized cost</u>	<u>Estimated fair value</u>
Within 1 year	\$ 83,731,252	\$ 83,933,825
After 1 year through 5 years	117,341,255	118,318,763
After 5 years through 10 years	73,531,101	73,281,325
After 10 years	<u>-</u>	<u>-</u>
	<u>\$ 274,603,608</u>	<u>\$ 275,533,913</u>

In lieu of purchasing a bond, as required by the Kentucky Department of Insurance, the Fund has pledged approximately \$28,191,616 and \$27,243,419 of investments, at fair value, as collateral for the payment of workers' compensation claims as of December 31, 2019 and 2018, respectively. The amount pledged is to remain under the joint control of the Fund and the Department of Insurance, for the exclusive payment of any liability for workers' compensation claims incurred by the Fund.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note C - Investments (Continued)

The following table shows the investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

	2019					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Treasury notes and bonds	\$ 85,801,963	\$ (32,962)	\$ 45,267,186	\$ (40,932)	\$ 131,069,149	\$ (73,894)
Domestic common stocks						
Basic material common stocks	-	-	1,263,268	(278,739)	1,263,268	(278,739)
Other common stocks and mutual funds	56,660,492	(669,796)	2,995,276	(631,519)	59,655,768	(1,301,315)
Corporate obligations	22,010,935	(2,640)	11,222,645	(2,221)	33,233,580	(4,861)
Municipal obligations	77,399,395	(168,293)	22,331,386	(163,129)	99,730,781	(331,422)
Total	\$241,872,785	\$ (873,691)	\$ 83,079,761	\$ (1,116,540)	\$ 324,952,546	\$ (1,990,231)
	2018					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Treasury notes and bonds	\$ 51,305,812	\$ (84,643)	\$ 69,627,284	\$ (1,312,469)	\$ 120,933,096	\$ (1,397,112)
Domestic common stocks						
Basic material common stocks	843,931	(180,232)	-	-	843,931	(180,232)
Financial institutions common stocks	1,995,900	(1,597)	-	-	1,995,900	(1,597)
Other common stocks and mutual funds	3,549,544	(1,107,781)	1,781,192	(563,718)	5,330,736	(1,671,499)
Corporate obligations	7,595,035	(76,492)	16,834,170	(256,019)	24,429,205	(332,511)
Municipal obligations	2,963,110	(34,541)	75,622,280	(2,323,397)	78,585,390	(2,357,938)
Total	\$ 68,253,332	\$ (1,485,286)	\$ 163,864,926	\$ (4,455,603)	\$ 232,118,258	\$ (5,940,889)

At December 31, 2019, seven municipal funds, one corporate bond, five other federal bonds with unrealized losses of \$163,129, \$2,221, and \$40,932, respectively, were in loss positions for 12 months or more. At December 31, 2018, thirty-two municipal funds, fourteen corporate bonds, two domestic common stocks and twenty-four U.S. treasury bonds with unrealized losses of \$2,323,397, \$76,492, \$563,718 and \$1,312,469, respectively, were in loss positions for 12 months or more. Based on consideration of various factors, such as the issuer credit quality of the bonds, likelihood of an event of default of the issuer, or government or other guarantee of principle, these assets presently do not meet the Fund's other-than-temporary asset impairment criteria and will not be impaired unless it meets the ASC impairment criteria in the future.

Bond fair values are subject to fluctuation based on, among other things, changes in interest rates. In a rising rate environment, bond values may experience a drop in market price which is normally recovered as the bond approaches its maturity date. The Fund has the intent and ability to hold all bond investments until recovery. At December 31, 2019, the Fund did not have the intent to sell any bonds whose fair value was less than amortized cost, it is not expected the Fund would be required to sell such securities, and the present values of the expected contractual future cash flows is sufficient to recover the entire amortized cost of the securities.

Note D - Excess Insurance

The Fund uses excess insurance agreements to limit its exposure on payment of claims. Excess Insurance permits recovery of a portion of claim losses from excess insurers and their reinsurers although it does not discharge the Fund from the primary liability as direct insurer.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note D - Excess Insurance (Continued)

Aggregate excess insurance provides coverage if the total losses of the Fund exceed certain percentages of earned premium. The Fund discontinued the purchase of aggregate excess coverage effective May 1, 1994 and has subsequently received an annual purchase waiver by fulfilling the requirements as set-forth by the Kentucky Department of Insurance. At December 31, 2019 and 2018, aggregate excess insurance receivables with an undiscounted value of \$544,088 were associated primarily with one excess insurer.

Specific excess insurance also provides coverage for each individual event loss in excess of certain amounts. At December 31, 2019 and 2018, specific excess insurance receivables with an undiscounted value of \$39,830,027 and \$29,285,094, respectively, were associated primarily with one excess insurer. The Fund does not hold any collateral under any excess insurance agreements. In the event that any of the excess insuring companies might be unable to meet their obligations under existing excess insurance agreements, the Fund would be liable for such amounts.

Note E - Estimated Liability for Claims

The following table provides a reconciliation of the reserve balance for losses and loss-adjustment expense from December 31, 2017 through December 31, 2019:

	<u>2019</u>	<u>2018</u>
Balance as of January 1	\$ 281,916,155	\$ 267,745,858
Less excess insurance receivables	<u>24,638,905</u>	<u>24,539,403</u>
Net balance as of January 1	<u>257,277,250</u>	<u>243,206,455</u>
Incurred related to		
Current year - undiscounted	53,122,800	58,574,600
Decrease in prior years' estimates - undiscounted	<u>(32,662,604)</u>	<u>(13,318,220)</u>
Total incurred - undiscounted	20,460,196	45,256,380
Paid related to		
Current year	7,083,790	6,965,725
Prior years	<u>24,623,864</u>	<u>24,219,860</u>
Total paid losses and LAE	<u>31,707,654</u>	<u>31,185,585</u>
Net balance as of December 31	246,029,792	257,277,250
Plus excess insurance receivables	<u>35,165,855</u>	<u>24,638,905</u>
Balance as of December 31	<u>\$ 281,195,647</u>	<u>\$ 281,916,155</u>
Effect of discounting reserves	\$ (17,758,023)	\$ (644,252)

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note E - Estimated Liability for Claims (Continued)

The discount rate at December 31, 2019 and 2018 is 1.8% and 2.5%, respectively. Discount rate is evaluated annually is determined by management and the Fund's actuary. The rate was lowered from 2.5% to 1.8% based on declining investment rates of return and the actuary's professional experience.

The following required supplementary information on page 17 and 18 includes incurred and paid loss development as of December 31, 2019, net of reinsurance, as well as cumulative claim frequency and the total of incurred-but-not reported liabilities, plus expected development on reported claims included within the net incurred claims amounts. The information about incurred and paid loss development for the years prior to 2017 is presented as supplementary information and is unaudited.

Note F - Income Taxes

The Fund's tax status is that of an insurance company subject to the provisions of Section 831 of the Internal Revenue Code of 1986, as amended. Under provisions of the Code, the Fund is permitted deductions for member dividends declared but not paid. The provision for federal income taxes is based upon an income tax return for the Fund as a stand-alone entity.

The tax effects of temporary differences, which give rise to deferred taxes at December 31, 2019 and 2018, are as follows:

	<u>2019</u>	<u>2018</u>
Deferred tax assets (liabilities)		
Estimated liability for claims	\$ 1,637,360	\$ 819,276
Net unrealized gains on investments	<u>(13,257,939)</u>	<u>(7,545,111)</u>
Net deferred tax liability	<u>\$ (11,620,579)</u>	<u>\$ (6,725,835)</u>

Income tax benefit for the years ended December 31, 2019 and 2018, consist of the following:

Current year (benefit) expense	\$ (6,756,241)	\$ 8,617,739
Deferred expense (benefit)	<u>4,003,119</u>	<u>(9,825,831)</u>
Income tax benefit	<u>\$ (2,753,122)</u>	<u>\$ (1,208,092)</u>

ASC Topic 740, *Income Taxes*, prescribes a recognition threshold and measurement attribute for the recognition, measurement, presentation, and disclosure of uncertain tax positions that the Fund has taken or expects to take on a tax return. ASC Topic 740 provides that a tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolution of any related appeals or litigation process, based on the technical merits of the income tax position.

Kentucky Associated General Contractors Self Insurers' Fund
Notes to Financial Statements (Continued)
Years Ended December 31, 2019 and 2018

Note F - Income Taxes (Continued)

As of December 31, 2019, there were no recorded uncertain tax positions. As of December 31, 2018, the Fund recorded a liability for an uncertain tax position of approximately \$6,272,000 as it related to its position with regard the repeal of Section 847. The uncertainty was resolved during 2019 and the liability was adjusted to income tax expense. The liability was reflected as a reduction of the related income tax receivable on the Fund's balance sheet. The Fund believes it is no longer subject to income tax examinations for years prior to 2016.

Note G - Related Party Transactions

Service fee expenses to Ladegast & Heffner Claims Service, Inc. were \$8,996,301 and \$8,327,035, for the years ended December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, service fee liabilities of \$1,080,554 and \$1,186,601, respectively, were due to Ladegast & Heffner Claims Service, Inc. The service fee is based on a percentage of premiums earned and was 13.7% at December 31, 2019 and 2018. During 2019, the Fund awarded an additional service fee to Ladegast & Heffner of \$101,667 monthly beginning January 2019 and ending December 2020.

Note H - Fund Balance

The Fund is required to maintain a minimum level of Fund Balance as set forth by the statutory requirements of the Kentucky Department of Insurance. The minimum requirement of \$1,000,000 was met as of December 31, 2019 and 2018, see note B6.

In 2019 and 2018, the Fund declared dividends of \$33,000,000 and \$11,000,000, respectively, recorded in accrued member dividends on the balance sheets.

Note I - Subsequent Events

In March 2020, the World Health Organization declared the global novel coronavirus disease 2019 (COVID-19) outbreak a pandemic. Further, the United States Centers for Disease Control and Prevention confirmed the spread of the disease throughout the United States, which is impacting businesses as well as financial markets. As of the date the financial statements were available to be issued, the Fund's operations have not been significantly impacted by the COVID-19 outbreak, however the Fund continues to experience fluctuations in the fair value of its investment portfolio, particularly investments in equity investments, and such fluctuations are impacting the Fund's Capital and Surplus subsequent to year end. The Fund's operations and the fair value of its investment portfolio could be adversely affected as a result of COVID-19, but the ultimate impact is not known at this point as the scale and severity of the outbreak, and resulting economic impact, is still largely unknown.

Required Supplementary Information

**Kentucky Associated General Contractors Self Insurers' Fund
Required Supplementary Information
Years Ended December 31, 2019 and 2018**

Workers compensation

Accident year	Ultimate loss (including IBNR) and allocated claim adjustment expenses, net of reinsurance										As of December 31, 2019	
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	IBNR (1)	Number of reported claims (2)
	Unaudited					Audited						
2010	\$ 49,815,320	\$ 49,720,001	\$ 50,367,743	\$ 50,029,479	\$ 50,062,529	\$ 48,555,447	\$ 49,679,560	\$ 48,229,091	\$ 47,790,935	\$ 46,447,905	\$ 5,123,400	2,892
2011		49,020,151	51,936,665	52,442,714	50,001,848	51,247,750	49,127,327	49,159,320	48,693,011	47,565,439	6,878,000	2,826
2012			52,137,981	49,939,942	49,499,884	48,890,150	47,877,256	46,904,365	45,392,631	43,618,395	7,029,200	2,857
2013				52,496,591	49,329,599	46,510,320	38,160,977	36,850,236	35,686,456	34,254,616	7,856,300	2,791
2014					56,148,591	56,048,310	55,496,852	52,498,680	50,702,492	48,130,311	8,715,700	2,748
2015						52,098,610	48,636,460	45,490,065	45,433,271	41,196,728	13,546,900	2,557
2016							55,501,662	51,983,275	52,004,940	48,955,058	14,604,800	2,702
2017								52,577,913	50,407,430	48,807,700	22,096,700	2,384
2018									58,574,600	52,144,500	21,909,500	2,291
2019										53,122,800	28,360,300	1,965
Total										\$ 464,243,452		

(1) Total of incurred-but-not-reported liabilities plus expected development on reported claims as of December 31, 2019.

(2) Claims frequency reported in the above table is determined on an individual claimant level.

Workers compensation

Accident year	Cumulative paid claims and allocated claim adjustment expenses, net of reinsurance									
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
	Unaudited					Audited				
2010	\$ 8,929,525	\$ 17,395,732	\$ 22,707,298	\$ 26,014,263	\$ 27,779,612	\$ 29,241,537	\$ 30,377,313	\$ 31,439,817	\$ 32,425,245	\$ 33,187,092
2011		9,167,050	18,318,650	23,812,713	27,199,545	29,261,084	30,739,537	32,019,368	33,409,274	34,366,566
2012			8,505,506	16,467,561	21,752,783	24,388,330	26,757,560	28,273,726	29,210,995	29,966,482
2013				6,913,295	13,829,311	17,956,581	20,757,371	22,255,058	22,808,556	23,273,056
2014					7,280,697	17,451,006	22,424,042	25,803,730	28,215,848	29,869,306
2015						6,758,910	12,887,596	16,032,862	17,972,982	19,649,692
2016							8,382,041	16,841,079	21,738,503	24,161,499
2017								6,210,014	13,063,429	16,915,721
2018									6,965,725	15,644,433
2019										7,083,790

Total paid net of reinsurance recoveries

234,117,637

All outstanding liabilities before 2010, net of reinsurance

57,550,634

Liabilities for claims and claim adjustment expenses, net of reinsurance \$ 287,676,449

**Kentucky Associated General Contractors Self Insurers' Fund
Required Supplementary Information (Continued)
Years Ended December 31, 2019 and 2018**

The reconciliation of the net incurred and paid loss development tables to the liability for losses and loss adjustment expenses in the balance sheet is as follows:

	<u>December 31, 2019</u>
Net outstanding liabilities	
Worker's compensation - case reserves	\$ 135,943,149
Worker's compensation - IBNR	147,507,469
Effect of discounting reserves	<u>(41,646,657)</u>
Discounted liabilities for unpaid claims and claim adjustment expenses, net of reinsurance	241,803,961
Excess reinsurance recoverable on unpaid claims	
Excess specific and aggregate	24,140,504
Excess IBNR	16,233,611
Effect of discounting recoverables	<u>(5,208,260)</u>
Total reinsurance recoverable on unpaid claims	35,165,855
Unallocated claims adjustment expenses	<u>4,225,831</u>
Total liabilities for unpaid claims and claim adjustment expenses	<u>\$ 281,195,647</u>

The following supplementary information is about the average historical claims duration as of December 31, 2019.

<u>Average Annual Percentage Payout of Incurred Claims by Age, Net of Reinsurance</u>										
Years	1	2	3	4	5	6	7	8	9	10
	16.6%	17.8%	10.4%	6.4%	4.5%	3.0%	2.2%	2.3%	2.1%	1.6%

The following is a summary of the liabilities for unpaid claims and claims adjustment expenses that are presented at fair value in the balance sheet as of December 31:

	<u>2019</u>	<u>2018</u>
Carrying amount of the liabilities for unpaid claims and claim adjustment expenses presented at fair value	\$281,195,647	\$281,916,155
Aggregate amount of discount	36,438,397	54,196,420
Range of interest rates used to discount	1-2%	2-3%