

**KENTUCKY WORKERS' COMPENSATION  
FUNDING COMMISSION**

**FINANCIAL STATEMENTS**

**AND**

**REPORT OF INDEPENDENT AUDITORS**

**JUNE 30, 2021**

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

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## REPORT OF INDEPENDENT AUDITORS

To the Board of Directors  
Kentucky Workers' Compensation Funding Commission

We have audited the accompanying financial statements of the Kentucky Workers' Compensation Funding Commission (the Funding Commission), as of and for the year ended June 30, 2021, and the related notes to the financial statements, which collectively comprise the Funding Commission's basic financial statements as listed in the table of contents.

### 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.

### Auditors' 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 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 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 auditors' 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.

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Funding Commission as of June 30, 2021, and the changes in its financial position, and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## Change in Accounting Principle

As described in Note 2 to the financial statements, the Funding Commission adopted Government Accounting Standards Board Statement No. 84 – *Fiduciary Activities*. Our opinion is not modified with respect to this matter.

## Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, on pages 3-10, the schedule of proportionate share of the net pension liability and the schedule of pension contributions on pages 44-45, and the schedule of proportionate share of the net OPEB liability and the schedule of OPEB contributions on pages 46-47, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental 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 because the limited procedures do not provide us with sufficient audit evidence to express an opinion or provide any assurance.

## Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 21, 2021, on our consideration of the Funding Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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* in considering the Funding Commission's internal control over financial reporting and compliance.

*Blue & Co., LLC*

Lexington, Kentucky  
September 21, 2021

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2021

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This narrative presents management's perspective of the fiscal year 2021 audit of the Special Fund, Coal Workers' Pneumoconiosis Fund (CWPF), and the Self Insurance Fund. We hope our analysis will help readers understand the financial position and results of operations for these restricted funds.

### **Highlights of Fiscal Year 2021**

- Investments of the Special Fund increased to approximately \$332.7 million at June 30, 2021 from approximately \$326.9 million at June 30, 2020, primarily as a result of reinvested investment income.

### **Kentucky Workers' Compensation Funding Commission**

#### Special Fund

The Kentucky Workers' Compensation Funding Commission (Funding Commission) was created through the enactment of House Bill No. 1 by the 1987 Extraordinary Session of the General Assembly, Commonwealth of Kentucky (Commonwealth) effective October 26, 1987, to act as an agency of the Commonwealth for the public purpose of controlling, investing, and managing the funds collected pursuant to House Bill No. 1, an act relating to workers' compensation. The Funding Commission collects workers' compensation Special Fund Assessments and uses such assessments to fund specific labor related programs, the Funding Commission, the Special Fund, and the Uninsured Employers' Fund. Accumulated assessments in excess of required transfers remain in the Benefit Reserve Fund and are invested in fixed income securities as recommended by the Funding Commission's investment advisory firm. In 2010, the General Assembly approved an extension of the sunset date from 2018 to 2029 for accumulating sufficient reserves to fund outstanding claims.

#### Coal Workers' Pneumoconiosis Fund

The CWPF was created through the enactment of House Bill No. 1 by the December 1996 Special Session of the General Assembly. The CWPF was originally established to be liable for one-half of the income benefits and retraining incentive benefits for pneumoconiosis claims with date of last exposure on or after December 12, 1996. To fund the pneumoconiosis claims, and to finance its administration and operation, assessments were imposed upon workers' compensation premiums received on or after January 1, 1997, through December 31, 2019 from employers, insurance carriers and self-insured engaged in the severance or processing of coal. An additional CWPF assessment was imposed on the tonnage of coal severed on or after January 1, 1997 through December 31, 2019. Pursuant to House Bill No. 377, An Act Relating to the Workers' Compensation Funding Commission, the CWPF ended its liability for income benefits for coal workers pneumoconiosis claims filed or reopened on or after July 1, 2017. Furthermore, the enacted bill mandated that all assets and liabilities of the CWPF be transferred to Kentucky Employers' Mutual Insurance (KEMI) through a loss portfolio transfer agreement, which occurred at the start of fiscal 2018. Assessments continue to be collected by the Funding Commission, which are subsequently transferred to KEMI after the end of each quarter. The

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2021

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Funding Commission has re-categorized the CWPf from a fiduciary fund to an enterprise fund during fiscal 2021 due to GASB 84. See Note 2.

### Self-Insurance Fund

The Self-Insurance Fund was established by Kentucky Revised Statute (KRS) 342.920 to protect employees of workers' compensation self-insured employers who had claims for injuries that occurred prior to the creation of the workers' compensation self-insurance guaranty funds. The Self-Insurance Fund was established for the purpose of making payments to workers' compensation claimants injured prior to March 1, 1997, when the security of a former self-insured employer has been depleted. All amounts collected after July 12, 2006, as fines and penalties under KRS 342.267 and 342.990 are paid into the Self Insurance Fund. The Department of Workers Claims has collected fines and penalties which have been remitted to the Funding Commission for the purpose of investment. The Funding Commission has established a custodial fund, the Self Insurance Fund, to account for the funds held and invested on behalf of the Department of Workers Claims.

### Financial Statements

The audited financial statements include a statement of net position, a statement of revenues, expenses, and changes in net position and a statement of cash flows for the year ended June 30, 2021. The Funding Commission financial statements are blended with the Department of Workers' Claims and add the outstanding claim liabilities for the Special Fund in the Commonwealth of Kentucky financial statements.

The statement of net position presents information on all of the Funding Commission's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Funding Commission is improving or deteriorating.

The statement of revenues, expenses, and changes in net position presents information showing how the Funding Commission's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The statement of cash flows provides relevant information about the cash receipts and cash payments of the Funding Commission during the fiscal year. The statement should help users assess the Funding Commission's ability to generate future net cash flows, meet future obligations as they become due, the Funding Commission's need for future external financing, the reasons for the differences in operating and related cash receipts and payments, and the effects on the financial position of cash and non-cash investing, capital, non-capital, and financing activities.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2021

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The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

### **Financial Analysis of the Funding Commission as a Whole**

Each of the funds managed by the Funding Commission are restricted for payment of specific types of claim liabilities. Therefore, an overall analysis of the Funding Commission financial statements must focus on each fund rather than the Funding Commission as a whole.

However, all investments of the Funding Commission are managed using the same Investment Policy Statement which establishes the following principles:

- Adherence to the "prudent man" rule that requires exercising that degree of judgment and care under the circumstances then prevailing which persons of prudence, discretion, and intelligence, who are familiar with such matters would follow in management of their own affairs in investment matters.
- Invest funds in a manner which will meet the unique objectives of each fund while minimizing the investment risk exposure of the funds; the primary goal being the safety of the principal and liquidity of the investments while providing the financial wherewithal to meet future benefit obligations.
- Utilize the Office of Financial Management and/or an investment consulting firm to provide expert, professional judgment related to investment decisions.
- Adoption of specific guidance for each category of assets to ensure a framework for monitoring quality, diversification, and liquidity.

Note 4 on pages 22 - 26 provides more details about risk management of the Funding Commission's investments. KRS 342.1223(2)(b) directs the Funding Commission to follow guidance in KRS Chapter 386 for investing the funds collected to finance the workers' compensation liabilities. KRS 386.020 outlines a variety of allowable investments for the funds administered by the Funding Commission.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2021

### **Financial Analysis of Restricted Funds**

#### Special Fund

Table 1 summarizes the net position of the Special Fund and Table 2 outlines the changes in net position for 2021 and 2020.

TABLE 1			
KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION SPECIAL FUND SUMMARY OF NET POSITION AS OF JUNE 30, 2021 AND 2020			
(In Thousands)			
	<b>2021</b>	<b>2020</b>	<b>PCT CHG</b>
Current assets	\$ 22,529	\$ 29,785	-24.4%
Restricted investments	332,740	326,907	1.8%
Total assets	355,269	356,692	-0.4%
Deferred outflows of resources	1,312	1,762	-25.5%
Total assets and deferrals	\$ 356,581	\$ 358,454	-0.5%
Current liabilities	\$ 1,373	\$ 1,366	0.5%
Long-term liabilities	8,690	8,838	-1.7%
Total liabilities	10,063	10,204	-1.4%
Deferred inflows of resources	336	345	
Total liabilities and deferrals	10,399	10,549	-1.4%
Restricted net position	\$ 346,182	\$ 347,905	-0.5%

Current assets decreased as a result of operating transfers exceeding operating income. Restricted investments increased due to the reinvestment of investment income, which was greater than the unrealized and realized losses recognized during the fiscal 2021. During the fiscal year, withdrawals from restricted investments were not required to fund operating transfers.



# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2021

TABLE 2			
KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION			
SPECIAL FUND SUMMARY OF CHANGES IN NET POSITION FOR THE YEARS ENDED JUNE 30, 2021 AND 2020			
(In Thousands)			
	2021	2020	PCT CHG
Operating revenues	\$ 63,535	\$ 67,777	-6.3%
Operating expenses	(1,829)	(2,326)	21.4%
Nonoperating revenues (expenses)	5,213	27,818	-81.3%
Transfers-claims	(40,131)	(46,823)	14.3%
Transfers-administrative costs	(28,510)	(30,004)	5.0%
Change in net position	\$ (1,722)	\$ 16,442	-110.5%

Operating revenues include assessments, penalties, and interest imposed as a result of audits of insurance companies and self-insured entities.

Transfers for both claims and administrative costs represent cash balances transferred to the Labor Cabinet to fund actual payments. In addition, claim transfers also include amounts remitted to the Attorney General's office for management of the Uninsured Employers Fund (claims and administrative costs). However, these amounts include changes in cash balances as well as shift in the underlying cost elements. Additional information about these amounts is provided in the Special Fund financial statements. Transfers to the Labor Cabinet and Kentucky Occupational Safety and Health were \$28.5 and \$30.0 million for each fiscal year ending in 2021 and 2020, respectively. These transfers are also based on the Commonwealth's Enacted Budget.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2021

### Coal Workers' Pneumoconiosis Fund

Table 3 summarizes the financial position of the CWPF and Table 4 outlines the changes in net position for 2021 and 2020.

TABLE 3			
<b>KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION</b>			
<b>COAL WORKERS' FUND SUMMARY OF NET POSITION AS OF JUNE 30, 2021 AND 2020</b>			
	(In Thousands)		PCT CHG
	2021	2020	
Current assets	\$ 882	\$ 2,526	-65.1%
Restricted investments	267	-0-	0.0%
Total assets	<u>\$ 1,149</u>	<u>\$ 2,526</u>	-54.5%
Current liabilities	\$ -0-	1,789	-100.0%
Restricted net position	<u>\$ 1,149</u>	<u>\$ 737</u>	55.9%

Assets in the CWPF decreased as a result of the transfers to KEMI and refunds paid during the year.

TABLE 4			
<b>KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION</b>			
<b>COAL WORKERS' FUND SUMMARY OF CHANGES IN NET POSITION FOR THE YEARS ENDED JUNE 30, 2021 AND 2020</b>			
	(In Thousands)		PCT CHG
	2021	2020	
Operating revenues	\$ (808)	2,666	-130.3%
Operating expenses	(269)	(102)	-163.7%
Nonoperating revenues (expenses)	1,489	(7,371)	120.2%
Change in net position	<u>\$ 412</u>	<u>\$ (4,807)</u>	108.6%

The Funding Commission earned CWPF assessments totaling \$(808,000) as a result of refunds and credits exceeding assessments earned, which is significantly less than the prior fiscal year and is expected as the CWPF approaches closure. Effective on January 1, 2020, the CWPF assessment and tonnage rates were set to 0% and \$0.00 cents per ton, respectively, since the related claims liability was actuarially determined to be fully funded. Accordingly, not only were transfers to KEMI of \$617,000 significantly less than the prior fiscal year, but the Funding Commission also received \$2.1 million from KEMI, which was refunded to insurers in the current fiscal year.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2021

### **Self-Insurance Fund**

Table 5 summarizes the financial position of the Self-Insurance Fund and Table 6 outlines the changes in net position for 2021 and 2020.

TABLE 5			
<b>KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION SELF INSURANCE FUND SUMMARY OF NET POSITION AS OF JUNE 30, 2021 AND 2020</b>			
	(In Thousands)		PCT CHG
	2021	2020	
Current assets	\$ 8,650	\$ 3,905	121.5%
Restricted investments	895	5,665	-84.2%
Total assets	<u>\$ 9,545</u>	<u>\$ 9,570</u>	-0.3%
Restricted net position	<u>\$ 9,545</u>	<u>\$ 9,570</u>	-0.3%

Restricted investments decreased as a result of selling three mutual funds in preparation for a change in investment strategy to begin in fiscal 2022.

TABLE 6			
<b>KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION SELF INSURANCE FUND SUMMARY OF CHANGES IN NET POSITION FOR THE YEARS ENDED JUNE 30, 2021 AND 2020</b>			
	(In Thousands)		PCT CHG
	2021	2020	
Penalty and interest collected for another government	\$ 589	\$ 885	-33.4%
Net investment earnings	185	317	-41.6%
Distributions to another government	(800)	(1,300)	38.5%
Change in net position	<u>\$ (26)</u>	<u>\$ (98)</u>	73.5%

The change in net position of the Self Insurance Fund decreased as a result of penalty funds received in the amount of \$589,172, interest and dividend income of \$76,481, and the change in market value of \$108,322, which were less than the amount of \$800,000 transferred out to pay claims.

### **Current Year's Budget**

The Funding Commission's operating budget, which includes transfers to Workers Claims, the Uninsured Employers Fund, Kentucky Occupational Safety and Health, and the Funding Commission (administrative expenses) for fiscal years 2021 and 2020 was \$97 million and \$107 million, respectively. Actual expenditures were \$71 million (73% of budget) in fiscal 2021 and \$79 million (74% of budget) in fiscal 2020.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2021

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### **Fiduciary Funds**

As described in Note 2 to the financial statements, the Funding Commission adopted Government Accounting Standards Board Statement No. 84 – *Fiduciary Activities* on July 1, 2020. Fiduciary funds are used to account for resources held for the benefit of individuals or units outside of the Funding Commission. The Funding Commission is the fiduciary responsible for the assets. The Funding Commission is responsible for ensuring that the assets reported in this fund are used for their intended purposes. All of the Funding Commission's fiduciary activities are reported in a separate statement of fiduciary net position and a statement of changes in fiduciary net position. The statement of fiduciary net position and the statement of changes in fiduciary net position can be found on pages 15 and 16, respectively, of this report.

### **Contacting the Funding Commission's Financial Management**

This discussion and analysis is intended to provide a general overview of the finances and operations of the Funding Commission. If further information is needed, please contact Kim C. Hay, Director of Fiscal Operations, Kentucky Workers' Compensation Funding Commission, 42 Mill Creek Park, Frankfort, KY 40601, 502-931-1110.

Sincerely,



Kim C. Hay  
Director of Fiscal Operations  
Funding Commission

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENTS OF NET POSITION

JUNE 30, 2021

	<u>Special Fund</u>	<u>Coal Workers' Pneumoconiosis Fund</u>	<u>Totals</u>
<b>Assets:</b>			
Current assets:			
Cash and cash equivalents	\$ 4,005,586	\$ 829,088	\$ 4,834,674
Accounts receivable	189,566	-0-	189,566
Assessments receivable	15,434,023	52,660	15,486,683
Accrued interest receivable	2,899,558	-0-	2,899,558
Total current assets	<u>22,528,733</u>	<u>881,748</u>	<u>23,410,481</u>
Restricted investments	<u>332,739,442</u>	<u>267,195</u>	<u>333,006,637</u>
Total assets	355,268,175	1,148,943	356,417,118
Deferred outflows of resources:			
Deferred outflows - pension	893,556	-0-	893,556
Deferred outflows - OPEB	418,932	-0-	418,932
Total deferred outflows of resources	<u>1,312,488</u>	<u>-0-</u>	<u>1,312,488</u>
Total assets and deferrals	<u>\$ 356,580,663</u>	<u>\$ 1,148,943</u>	<u>\$ 357,729,606</u>
<b>Liabilities:</b>			
Current liabilities:			
Accrued expenses	\$ 571,160	\$ -0-	\$ 571,160
Compensated absences	86,938	-0-	86,938
Refunds payable	714,648	-0-	714,648
Total current liabilities	<u>1,372,746</u>	<u>-0-</u>	<u>1,372,746</u>
Noncurrent liabilities:			
Long-term compensated absences	20,468	-0-	20,468
Net pension liability	7,351,597	-0-	7,351,597
Other post-employment benefits liability	1,317,719	-0-	1,317,719
Total noncurrent liabilities	<u>8,689,784</u>	<u>-0-</u>	<u>8,689,784</u>
Total liabilities	10,062,530	-0-	10,062,530
Deferred inflows of resources:			
Deferred inflows - pension	144,462	-0-	144,462
Deferred inflows - OPEB	191,677	-0-	191,677
Total deferred inflows of resources	<u>336,139</u>	<u>-0-</u>	<u>336,139</u>
Total liabilities and deferrals	<u>10,398,669</u>	<u>-0-</u>	<u>10,398,669</u>
<b>Net Position:</b>			
Restricted	<u>\$ 346,181,994</u>	<u>\$ 1,148,943</u>	<u>\$ 347,330,937</u>

*See accompanying notes to the financial statements.*

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION YEAR ENDED JUNE 30, 2021

	Special Fund	Coal Workers' Pneumoconiosis Fund	Totals
<b>Operating revenues:</b>			
General assessments	\$ 61,209,549	\$ (808,045)	\$ 60,401,504
Penalty and interest income	2,038,483	-0-	2,038,483
Audit reimbursements	287,267	-0-	287,267
Total operating revenues	63,535,299	(808,045)	62,727,254
<b>Operating expenses</b>	1,828,738	269,324	2,098,062
<b>Net operating income (loss)</b>	61,706,561	(1,077,369)	60,629,192
<b>Nonoperating revenues (expenses):</b>			
Net decrease in the fair value of investments	(6,596,412)	-0-	(6,596,412)
Interest revenue	11,809,786	5,291	11,815,077
Net payment from Kentucky Employers' Mutual Insurance	-0-	1,483,279	1,483,279
Total nonoperating revenues (expenses)	5,213,374	1,488,570	6,701,944
<b>Income before operating transfers</b>	66,919,935	411,201	67,331,136
<b>Operating transfers:</b>			
Workers' compensation payments:			
Office of workers claims	(36,135,900)	-0-	(36,135,900)
Uninsured employers fund	(3,995,100)	-0-	(3,995,100)
Administrative expenses:			
Labor Cabinet	(27,839,800)	-0-	(27,839,800)
Kentucky Occupational Safety and Health	(670,800)	-0-	(670,800)
Total operating transfers	(68,641,600)	-0-	(68,641,600)
<b>Changes in net position</b>	(1,721,665)	411,201	(1,310,464)
<b>Net position, beginning of year (as restated for CWPF)</b>	347,903,659	737,742	348,641,401
<b>Net position, end of year</b>	\$ 346,181,994	\$ 1,148,943	\$ 347,330,937

*See accompanying notes to the financial statements.*

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENTS OF CASH FLOWS YEAR ENDED JUNE 30, 2021

	Special Fund	Coal Workers' Pneumoconiosis Fund	Totals
<b>Operating activities:</b>			
Assessments collected:			
Special Fund-public	\$ 60,779,032	\$ (1,835,921)	\$ 58,943,111
Special Fund-state	1,406,331	-0-	1,406,331
Penalty and interest collected	2,264,567	-0-	2,264,567
Audit expense reimbursements	287,267	-0-	287,267
Cash payments for:			
Refunds	(1,196,941)	-0-	(1,196,941)
Goods and services	(309,872)	(768,781)	(1,078,653)
Employee salaries and benefits	(1,199,637)	-0-	(1,199,637)
<b>Net cash flows from operating activities</b>	62,030,747	(2,604,702)	59,426,045
<b>Noncapital financing activities:</b>			
Operating transfers to:			
Workers compensation claims	(40,131,000)	-0-	(40,131,000)
Labor Cabinet	(27,839,800)	-0-	(27,839,800)
Kentucky Occupational Safety and Health Review Commission	(670,800)	-0-	(670,800)
Payment from Kentucky Employers' Mutual Insurance	-0-	1,483,279	1,483,279
<b>Net cash used in noncapital financing activities</b>	(68,641,600)	1,483,279	(67,158,321)
<b>Investing activities:</b>			
Investment income	11,766,914	5,291	11,772,205
Investment purchases	(101,272,313)	(267,194)	(101,539,507)
Investment sales and maturities	89,074,565	-0-	89,074,565
<b>Net cash flows from investing activities</b>	(430,834)	(261,903)	(692,737)
<b>Net change in cash and cash equivalents</b>	(7,041,687)	(1,383,326)	(8,425,013)
<b>Cash and cash equivalents, beginning of year</b>	11,047,273	2,212,414	13,259,687
<b>Cash and cash equivalents, end of year</b>	\$ 4,005,586	\$ 829,088	\$ 4,834,674

*See accompanying notes to the financial statements.*

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENTS OF CASH FLOWS YEAR ENDED JUNE 30, 2021

	<b>Special Fund</b>	<b>Coal Workers' Pneumoconiosis Fund</b>	<b>Totals</b>
<b>Reconciliation of net operating income (loss) to net cash flows from operating activities</b>			
Net operating income (loss)	\$ 61,706,561	\$ (1,077,369)	\$ 60,629,192
Adjustments to reconcile net operating income (loss) to net cash flows from operating activities			
(Increase) decrease in:			
Accounts receivable	141,311	-0-	141,311
Assessments receivable	115,907	63,104	179,011
Interfund receivable	-0-	198,188	198,188
Deferred outflows	449,843	-0-	449,843
Increase (decrease) in:			
Accrued expenses	20,370	(499,457)	(479,087)
Compensated absences	23,290	-0-	23,290
Refunds payable	(54,073)	(1,289,168)	(1,343,241)
Interfund payable	(198,188)	-0-	(198,188)
Deferred inflows	(9,449)	-0-	(9,449)
Other post-employment benefits liability	116,355	-0-	116,355
Net pension liability	(281,180)	-0-	(281,180)
<b>Net cash flows from operating activities</b>	<b>\$ 62,030,747</b>	<b>\$ (2,604,702)</b>	<b>\$ 59,426,045</b>
<b>Supplemental disclosure of noncash investing activities:</b>			
Net change in fair value of investments	\$ (6,596,412)		
Due to broker within accrued expenses exchanged for investments	\$ 325,000		

*See accompanying notes to the financial statements.*



# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENT OF FIDUCIARY NET POSITION—CUSTODIAL FUND JUNE 30, 2021

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	<b>Self Insurance Fund</b>
<b>Assets:</b>	
Current assets:	
Cash and cash equivalents	\$ 8,622,780
Penalty receivable	27,086
Accrued interest receivable	17
Total current assets	<u>8,649,883</u>
Other assets:	
Investments	<u>894,785</u>
<b>Total assets</b>	<u><u>\$ 9,544,668</u></u>
<b>Net Position:</b>	
Restricted for:	
Organizations and other governments	<u><u>\$ 9,544,668</u></u>

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*See accompanying notes to the financial statements.*

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## STATEMENT OF CHANGES IN FIDUCIARY NET POSITION—CUSTODIAL FUND YEAR ENDED JUNE 30, 2021

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	<b>Self Insurance Fund</b>
<b>Additions:</b>	
Penalty and interest	589,172
Investment earnings:	
Net increase in the fair value of investments	108,322
Interest	76,481
Total investment earnings	<u>184,803</u>
Total additions	<u>773,975</u>
<b>Deductions:</b>	
Distributions to other organization	<u>800,000</u>
Total deductions	<u>800,000</u>
Change in net position	(26,025)
<b>Net Position - Beginning of year, as restated</b>	<u>9,570,693</u>
<b>Net Position - end of year</b>	<u><u>\$ 9,544,668</u></u>

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*See accompanying notes to the financial statements.*

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### 1. GENERAL INFORMATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Kentucky Worker's Compensation Funding Commission

The Kentucky Workers' Compensation Funding Commission (Funding Commission) was created by Kentucky Revised Statute (KRS) 342.1223 effective October 26, 1987, to act as an agency of the Commonwealth of Kentucky (Commonwealth) for the public purpose of controlling, investing and managing the funds collected pursuant to KRS 342.1222. The Funding Commission collects workers' compensation Special Fund assessments and transfers such amounts as are necessary to pay administrative expenses and current claims of the Workers' Compensation Special Fund (Special Fund) and the Uninsured Employers' Fund. Accumulated Special Fund assessments in excess of required transfers remain in the Benefit Reserve Fund of the Funding Commission. The Funding Commission also collects Coal Workers' Pneumoconiosis Fund (CWPF) assessments, which are required to be transferred to Kentucky Employers' Mutual Insurance (KEMI) Authority each quarter.

#### Special Fund

The assessments authorized by the enabling legislation are intended to generate an amount projected to provide sufficient cash reserves to fund the Commonwealth's workers' compensation subsequent injury liability incurred prior to December 12, 1996, the liabilities of the Commonwealth's Uninsured Employers' Fund, plus the payment of various administrative costs for the Labor Cabinet. These assessments are accumulated and reported in the Special Fund in the accompanying financial statements. In accordance with KRS 342.122, the Funding Commission shall impose annually a Special Fund assessment rate, which was 7.02% and 6.41% for calendar years 2021 and 2020, respectively, upon the amount of workers' compensation premiums received by insurance carriers writing workers' compensation insurance in the Commonwealth, by every group of self-insurers operating under the provisions of KRS 342.350(4) and against the premium, as defined in KRS 342.0011, of every employer carrying his or her own risk. Each calendar year, the Funding Commission shall adjust the Special Fund assessment rate to produce enough revenue to amortize, on a level basis, the projected liability of the Special Fund. In January 2010, the Kentucky General Assembly revised this statute to extend the sunset date for achieving full-funded status from December 31, 2018, to December 31, 2029.

#### Coal Workers' Pneumoconiosis Fund

The CWPF was created within the Labor Cabinet through the enactment of KRS 342.1242 by the December 1996 Special Session of the General Assembly. The CWPF was established to be liable for one-half of the income benefits and retraining incentive benefits for pneumoconiosis resulting from exposure to coal dust created in the severance or processing of coal. The employer was liable for the remaining one-half.

To fund and prefund the pneumoconiosis claims, and to finance its administration and operation, an assessment was imposed upon workers' compensation premiums and tonnage of coal severed on or

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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after January 1, 1997 through December 31, 2019, from employers, insurance carriers and self-insured companies engaged in the severance or processing of coal.

On April 10, 2017, Kentucky House Bill No. 377, *An Act Relating to the Workers Compensation Funding Commission*, was signed into law by the Governor. The provisions in the bill closed the CWPF effective July 1, 2017, to any coal workers' pneumoconiosis claims filed after June 30, 2017. Assets and liabilities of the Kentucky Coal Workers Pneumoconiosis Fund were transferred through a loss portfolio transfer agreement to KEMI, which is a nonprofit, independent, self-supporting municipal corporation and political subdivision of the Commonwealth. Under the provisions of the loss portfolio transfer agreement, the Funding Commission will continue to collect assessments for the CWPF and forward them to KEMI. KEMI may also transfer funds to the CWPF as needed to cover refunds, credits, and settlements. KEMI transferred \$2.1 million to the CWPF for such purposes, and the CWPF transferred \$617,000 to KEMI in collected assessments during fiscal 2021. Furthermore, the Funding Commission has re-categorized the CWPF from a fiduciary fund to an enterprise fund due to the Government Accounting Standards Board's (GASB) Statement No. 84. See Note 2.

### Self-Insurance Fund

The Self-Insurance Fund was established by KRS 342.920 to protect employees of workers' compensation self-insured employers who had claims for injuries that occurred prior to the creation of the workers' compensation self-insurance guaranty funds. The Self-Insurance Fund was established for the purpose of making payments to workers' compensation claimants injured prior to March 1, 1997, when the security of a former self-insured employer has been depleted.

All amounts collected after July 12, 2006, as fines and penalties under KRS 342.267 and 342.990 are paid into the Self-Insurance Fund. The Department of Claims has collected fines and penalties which have been remitted to the Funding Commission for the purpose of investment. The Funding Commission has established a custodial fund, the Self-Insurance Fund, to account for the funds held and invested.

### Reporting Entity

The Funding Commission's activities are combined with the workers' compensation liability and activity of the Special Fund and the Uninsured Employers' Fund and accounted for by the Commonwealth in a public entity risk sharing pool in the Commonwealth's Annual Comprehensive Financial Report (ACFR).

### Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for state governments as prescribed by the GASB. The Special Fund and CWPF are presented as enterprise funds and are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The Kentucky Workers' Compensation Funding Commission reports the Special Fund and the CWPFF as the only major proprietary funds.

Additionally, the Funding Commission reports the Self-Insurance Fund as a custodial fund, which account for funds held for custodial purposes only. The custodial fund is reported using the economic resources measurement focus and the accrual basis of accounting. The recognition of certain liabilities to beneficiaries occur when an event compels the government to disburse fiduciary resources such as when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Kentucky Workers' Compensation Funding Commission are assessments levied on insurance companies and employers. Operating expenses for proprietary funds include administrative expenses. Non-operating revenues and expenses include investment related transactions, including net changes in fair values, management fees, interest, and dividend income. Transfers to fund workers' compensation claims and Labor Cabinet administrative expenses are also segregated in the statement of revenues, expenses, and changes in net position.

### Use of Estimates

The preparation of financial statements in accordance 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 the related disclosures. Certain estimates relate to unsettled transactions and events as of the date of the financial statements. Other estimates relate to assumptions about the ongoing operations and may impact future periods. Accordingly, upon settlement, actual results could differ from estimated amounts.

### Description of Net Position Classes

*Restricted* net position is a component of net position with constraints placed on net position used through external restrictions imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or limitations imposed by law through constitutional provisions or enabling legislation. All assets of the Funding Commission's proprietary fund are restricted by enabling legislation in KRS 342.1227, 342.1242, and 393.080 for the payment of workers' compensation claims or Labor Cabinet administrative expenses.

*Net investment in capital assets* is a component of net position that consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.

*Unrestricted* net position is a component of net position that does not meet the definition of "restricted" or "net investment in capital assets." However, all assets of the Funding Commission meet the definition of restricted net position.

### Cash and Cash Equivalents

The Funding Commission considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents.

### Accounts Receivable

Accounts receivables are reported at their net invoice amounts and are reduced by the estimated portion that is expected to be uncollectible, if appropriate. At June 30, 2021, management considered all receivables to be fully collectible. Accordingly, there was no allowance for uncollectible receivables.

Certain receivables result from premium audits performed by the Funding Commission. A receivable is recognized on all finalized premium audits where the amounts due for additional assessments, penalty, interest, and audit expenses are not in protest. Receivables are not recognized on premium audits where the amount due is under protest by the insurance carrier or self-insurer.

### Assessments Receivable

Assessments receivable consists of amounts outstanding at the end of the year and expected to be collected within sixty days of the fiscal year-end.

### Investments

Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of net position. Changes in the fair value of investments are included in the change in net position in the accompanying statement of revenues, expenses, and changes in net position.

### Operating and Nonoperating Revenues

The Funding Commission defines operating revenues as revenues incurred through the normal operations of the Funding Commission, which includes the premium assessments, penalties and interest, and billings for audit cost reimbursements. Non-operating revenues include investment earnings and changes in fair value, as well as transfers from other funds of the Commonwealth.

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### Pension and Post-employment Benefits Other Than Pensions (OPEB)

For purposes of measuring the net pension and OPEB liabilities, deferred outflows of resources and deferred inflows of resources related to the pension and OPEB, and pension and OPEB expense, information about the fiduciary net position of the Kentucky Employees' Retirement System (KERS) and addition to/deductions from KERS's fiduciary net position have been determined on the same basis as they are reported by the Funding Commission.

KERS recognizes benefit payments (including refunds of employee contributions) when due and payable in accordance with the benefit terms. Investments are reported at fair value, except for money market investments and participating interest earning investment contracts that have a maturity at the time of purchase of one year or less, which are reported at cost. The KERS Non-hazardous Insurance Funds are reported as OPEB trust funds and are accounted for on the accrual basis of accounting.

### Fiduciary Funds

Following the Funding Commission's financial statements are separate financial statements for fiduciary funds. Fiduciary funds are excluded from the Funding Commission's financial statements as these assets are held in a custodial capacity for the various outside organizations and cannot be used to support the Funding Commission's programs. The Funding Commission's Self-Insurance Fund is reported under the fiduciary funds.

## **2. CHANGE IN ACCOUNTING PRINCIPLE**

On July 1, 2020, the Funding Commission adopted GASB Statement No. 84 – *Fiduciary Activities*. Generally, this statement requires governmental entities, who control assets of a fiduciary activity in which a fiduciary relationship exists with beneficiaries, to include those activities in two separate, interrelated financial statements, the statement of fiduciary net position and the statement of changes in fiduciary net position. Prior to the adoption of this statement, only the statement of fiduciary net position was presented for the Funding Commission's fiduciary funds, and those funds did not report any net position at June 30, 2020. The changes adopted to conform to the provisions of this statement were applied by restating the beginning net position of the CWPF to \$737,742 and the Self-Insurance Fund to \$9,570,693. Further, the Funding Commission has re-categorized the CWPF from a fiduciary fund to an enterprise fund.

## **3. CASH AND CASH EQUIVALENTS**

A portion of the restricted cash and cash equivalents managed by the Funding Commission are part of the Commonwealth's cash and investments pool, which has statutory responsibility and authority to safeguard the funds. Legally authorized investments generally include obligations of or guaranteed by the United States; obligations of any corporation of the United States Government; asset backed

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

securities; U.S. dollar denominated corporate securities; collateralized certificates of deposit; bankers' acceptances; commercial paper; and repurchase agreements. The Commonwealth is also eligible to engage in reverse repurchase agreements. See the Commonwealth's Comprehensive Annual Financial Report for the year ended June 30, 2021, for disclosure of the credit risk classifications of the cash and investment pool.

As of June 30, 2021, cash and cash equivalents consist of the following:

	<b>Special Fund</b>	<b>CWPF</b>	<b>Custodial Fund Self Insurance Fund</b>
Deposits in state pool	\$ 2,335,695	\$ 829,088	\$ 2,776,458
State Street Institutional Liquid Reserves Fund	1,669,891	-0-	5,846,322
	<b>\$ 4,005,586</b>	<b>\$ 829,088</b>	<b>\$ 8,622,780</b>

#### 4. INVESTMENTS

##### Investment Policy

KRS 342.1223(2)(b) directs the Funding Commission to follow guidance in KRS Chapter 386 for investing the funds collected to finance the workers' compensation liabilities. KRS 386.020 outlines a variety of allowable investments for the funds administered by the Funding Commission. The Funding Commission uses the services of an investment consulting firm.

In November 2018, the Funding Commission Board of Directors updated their Investment Policy Statement which provides more specific guidance for staff, investment counsel, and individual investment managers. The Directors' Policy Statement is based on the following key principles:

- Adherence to the "prudent man" rule that requires exercising that degree of judgment and care under the circumstances then prevailing which persons of prudence, discretion, and intelligence, who are familiar with such matters would follow in management of their own affairs in investment matters.
- Invest funds in a manner which will meet the unique objectives of each fund while minimizing the investment risk exposure of the funds; the primary goal being the safety of the principal and liquidity of the investments while providing the financial wherewithal to meet future benefit obligations.
- Utilize the Office of Financial Management and/or an investment consulting firm to provide expert, professional judgment related to investment decisions.
- Adoption of specific guidance for each category of assets to ensure a framework for monitoring quality, diversification, and liquidity.



# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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The Investment Policy Statement also provides specific guidance for investment managers regarding reporting and other communications, diversification, risk management, asset allocation, statutory restrictions, safety, liquidity, and total return goals, plus a list of authorized investments. Authorized investments outlined in the Investment Policy Statement include:

*Fixed Income Securities:*

- United States Treasury securities, agencies, and other obligations backed by the full faith and credit of the United States Government.
- United States Government and United States Government Agency guaranteed mortgage pools.
- Bank Certificates of Deposit rated A or better by a recognized rating service; limited to no more than 5% of the total fund assets.
- Domestic and foreign corporate obligations with investment grade ratings by a recognized rating service at the time of purchase.
- Bankers' Acceptances which originated by a bank rated in one of the top 3 rating categories by a recognized rating service, subject to a limitation of 10% of fund assets and no more than 2.5% in a single issue. However, the combined total of Banker's Acceptances and Commercial paper will not exceed 10% of total fund assets.
- Repurchase Agreements, collateralized at 102% of market value with United States Treasuries and agencies. These agreements must be governed by the Public Securities Association Master Repurchase Agreement.
- Money Market accounts and Mutual Funds approved by the Board.
- Investments not subject to KRS 342.1227.
- Other investments as approved by the Funding Commission.

*Equity:*

- Each manager's portfolio will hold at least 20 positions.
- No single issuer shall exceed 12 percent of the manager's portfolio at cost or 15 percent at market.
- There shall be no purchase which would cause a position in the portfolio to equal or exceed five percent of the issue outstanding.
- Non-marketable securities are not allowed.
- Derivatives are generally excluded for risk management or leveraging positions.

Balances among the asset classes and the percentages of the Special Fund, CWPF, and Self-Insurance Fund portfolios as of June 30, 2021 are outlined in the following table:

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

<b>INVESTMENT ALLOCATIONS</b>		
<b>Types of Securities</b>	<b>June 30, 2021</b>	
	<b>Balance</b>	<b>Percentage</b>
<u>Enterprise:</u>		
Special Fund:		
Fixed income	\$331,987,766	99.8%
Investments in state pool	751,676	0.2%
Restricted investments	\$332,739,442	100.0%
CWPF:		
Investments in state pool	\$ 267,195	100.0%
<u>Custodial:</u>		
Self-Insurance Fund:		
Investments in state pool	\$ 894,785	100.0%

### Interest Rate Risk

Interest rate risk is the risk that changes in interest rates of investments will adversely affect the fair value of an investment. The following investment tables outline the weighted average maturities for each category of investments held by the respective funds. Fixed income security performance is evaluated against various Barclay's indices net of management fees. The Funding Commission has elected to use the duration method to outline the potential interest rate risk in the fixed income portfolio. The Investment Policy Statement requires managers to maintain their portfolio's effective duration within 25% of the benchmark's effective duration. The following table details the effective duration by investment type for each investment in the fixed income portfolio of the Special Fund and Self-Insurance Fund.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

<b>INTEREST RATE RISK</b>		
<b>Investment Type</b>	<b>Fair Value</b>	<b>Effective Duration</b>
<u>Enterprise:</u>		
Special Fund:		
Corporate Bonds	\$167,425,851	6.62
U.S. Treasury Notes and Bonds	67,429,043	7.41
Taxable Municipals	40,431,763	7.99
U.S. Agency Mortgage-Backed Securities	23,045,328	2.68
Asset Backed Securities	16,645,113	3.58
Collateralized Mortgage Obligations	11,437,126	7.76
Collateralized Mortgage-Backed Securities	5,243,673	6.14
Local Government	329,869	12.94
Total Special Fund Fixed Income Securities	\$331,987,766	

### Credit Risk of Securities

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The investment policy limits credit risks on investments by prescribing allowable credit ratings for specific types of investments as described above. The following investment tables present the credit ratings for each investment type held in the fixed income portfolio by the respective funds.

<b>CREDIT RISK</b>			
<b>Investment Type</b>	<b>Market Value</b>	<b>Ratings</b>	<b>Percent</b>
<u>Enterprise:</u>			
Special Fund:			
Corporate Bonds	\$167,425,851	BBB- through AA	50.4%
U.S. Treasury Notes and Bonds	67,429,043	U. S. Treasuries	20.3%
Taxable Municipals	40,431,763	A through AAA	12.2%
U.S. Agency Mortgage-Backed Securities	23,045,328	AAA	6.9%
Asset Backed Securities	16,645,113	A- through AAA	5.0%
Collateralized Mortgage Obligations	11,437,126	AAA	3.4%
Collateralized Mortgage-Backed Securities	5,243,673	A- through AA-	1.6%
Local Government	329,869	AA-	0.1%
Total Special Fund Fixed Income Securities	\$331,987,766		100.0%

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Funding Commission's investment policy specifically outlines a strategy to manage the concentration of credit risk:

- Other than specified below, the maximum allocations per issuer by credit ratings for corporate bonds, non-agency residential and commercial backed mortgages and asset backed securities as follows: AAA, 5%; AA, 4%; A, 3%; and BBB, 2%.
- No more than 10% of the total fund may be invested in any one U.S. government agency issuer.
- No more than 3% of the total fund may be invested in any one issue of a GNMA mortgage-backed security or agency mortgage-backed security.
- No more than 10% of the total fund may be invested in securities of foreign countries.

### Custodial Credit Risk

For an investment, custodial credit risk is the risk that in the event of failure of the counter party, the Funding Commission will be able to recover the value of its investments or collateral securities that are in possession of an outside party. As of June 30, 2021, the Funding Commission's investments are either insured or held by the Funding Commission's custodian in the Funding Commission's name.

## 5. COMPENSATED ABSENCES

The policy of the Funding Commission is to record the cost of annual and compensatory leave. Annual leave is accumulated at amounts ranging from 7.50 to 15.00 hours per month, determined by length of service, with a maximum carry forward ranging from thirty to sixty days. The calendar year is the period used for determining accumulated leave. Compensatory leave is granted to authorized employees. It is the policy of the Funding Commission to record the cost of sick leave when paid. Generally, sick leave (earned one day per month with unlimited accumulation) is paid when an employee is absent due to illness, injury, or related family death. Sick leave accumulated is added to an employee's years of service at the time of retirement. There was no liability recorded for sick leave at June 30, 2021. The estimated accumulated amount of unused sick leave at June 30, 2021 for the Funding Commission was \$82,390.

Changes in compensated absences for the year ended June 30, 2021 are summarized as follows:

<b>Change in Compensated Absences</b>				
Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
\$ 84,116	\$ 89,250	\$ 65,960	\$ 107,406	\$ 86,938

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### **6. ACCOUNTS RECEIVABLE AND REFUNDS PAYABLE**

As discussed in Note 1, certain receivables result from premium audits performed by the Funding Commission. A receivable is recognized on all finalized premium audits where the amounts due for additional assessments, penalty, interest, and audit expenses are not in protest. Receivables are not recognized on premium audits where the amount due is under protest by the insurance carrier or self-insurer. As of June 30, 2021, there was approximately \$900,000 in audit assessments outstanding for non-finalized premium audits under protest for which no receivable or revenue has been recognized in the accompanying financial statements.

General and special assessments previously collected may become refundable as a result of premium audits and claim settlements. At June 30, 2021, there were approximately \$715,000 in refunds payable accrued as a result of premium audits in the Special Fund.

In addition to refunds paid as a result of premium audits, refunds of previously paid assessments may also be requested by insurance carriers for various reasons including errors in previous assessments calculations or adjustments to previously reported premiums. These requests are generally deducted immediately from the next quarterly assessments without prior approval and are verified by the Funding Commission through subsequent premium audits. Accordingly, at June 30, 2021, refund requests have been deducted from assessments collected for which the approval process has not been completed. However, no receivable or liability has been accrued since the amount ultimately to be approved cannot be reasonably estimated.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

### 7. RETIREMENT PLANS

All employees who work more than one hundred hours per month participate in a defined benefit plan administered by the Kentucky Employees Retirement System (KERS), a cost-sharing multi-employer public employee retirement system per Kentucky Revised Statute 61.565(3).

	<b>Tier 1</b> Participation Prior to 9/1/2008	<b>Tier 2</b> Participation 9/1/2008 through 12/31/2013	<b>Tier 3</b> Participation on or after 1/1/2014
<b>Covered Employees:</b>	Substantially all regular full-time members employed in non-hazardous and hazardous duty positions of any state department, board, or any agency directed by Executive Order to participate in KERS.		
<b>Benefit Formula:</b>	Final Compensation X	Benefit Factor X	Cash Balance Plan
	Service	Years of	
<b>Final Compensation:</b>	Average of the highest 5 fiscal years (must contain at least 48 months). Includes lump-sum compensation payments (before and at retirement).	5 complete fiscal years immediately preceding retirement; each year must contain 12 months. Lump-sum compensation payments (before and at retirement) are not to be included in creditable compensation.	No Final Compensation.
<b>Benefit Factor:</b>	1.97% - If you do not have 13 months' credit for 1/1/1998 - 1/1/1999. 2.00% - If you have 13 months' credit for 1/1/1998 - 1/1/1999.	10 years or less = 1.10%. Greater than 10 years, but no more than 20 years = 1.30%. Greater than 20 years, but no more than 26 years = 1.50%. Greater than 26 years, but no more than 30 years = 1.75%. Additional years above 30 = 2.00% (2.00% benefit factor only applies to service earned in excess of 30 years).	No benefit factor. A life annuity can be calculated in accordance with actuarial assumptions and a method adopted by the board based on member's accumulated account balance.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

	<b>Tier 1</b> Participation Prior to 9/1/2008	<b>Tier 2</b> Participation 9/1/2008 through 12/31/2013	<b>Tier 3</b> Participation on or after 1/1/2014
<b>Cost of Living Adjustment (COLA):</b>	No COLA unless authorized by the Legislature with specific criteria. This impacts all retirees regardless of Tier.		
<b>Unreduced Retirement Benefit:</b>	Any age with 27 years of service. Age 65 with 48 months of service. Money Purchase for age 65 with less than 48 months based on contributions and interest.	Rule of 87: Member must be at least age 57 and age plus earned service must equal 87 years at retirement to retire under this provision. Age 65 with 5 years of earned service. No Money Purchase calculations.	
<b>Reduced Retirement Benefit:</b>	Any age with 25 years of service. Age 55 with 5 years of service.	Age 60 with 10 years of service. Excludes purchased service (exception: refunds, omitted, free military).	No reduced retirement benefit.

Benefit and contribution rates are established by the state statute. Per KRS 61.565, contribution requirements of active employees and participating organization are established and may be amended by the Kentucky Retirement System's board. For the fiscal year ended June 30, 2021, Funding Commission employees were required to contribute 5 percent of their annual covered salary for retirement benefits. The Funding Commission was contractually required to contribute 73.28 percent of covered payroll to the nonhazardous KERS pension plan. Actuarially determined as an amount that, when combined with employee contributions, is expected to finance the cost and benefit earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The Funding Commission's total contributions to the KERS nonhazardous pension plan for the year ended June 30, 2021 were \$558,073.

In accordance with Senate Bill 2, signed by the Governor of Kentucky on April 4, 2013, plan members who began participating on, or after, January 1, 2014, are required to contribute to the Cash Balance Plan. The Cash Balance Plan is known as a hybrid plan because it has characteristics of both a defined benefit plan and a defined contribution plan. Members in the plan contribute 5% of their creditable compensation each month to their own account, and 1% to the Insurance Fund which is not credited to the member's account and is not refundable. The employer contribution rate is set annually by the Board of Trustees of the Kentucky Retirement Systems based on an actuarial valuation. The employer

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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contributes a set percentage of the member's salary. Each month, when employer contributions are received, an employer pay credit of 4% is deposited to the member's account. The employer pay credit represents a portion of the employer contribution.

At June 30, 2021, the Funding Commission reported a liability of \$7,351,597 for its proportionate share of net pension liability. The net pension liability was measured as of June 30, 2020, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2019, rolled forward to 2020 using generally accepted actuarial principles. The Funding Commission's proportion of the net pension liability was based on a projection of the Funding Commission's long-term share of contributions to the pension plan relative to the projected contributions of all participating entities. At June 30, 2021, the Funding Commission's proportion was 0.051901 percent.

The Board of Trustees adopted new actuarial assumptions since June 30, 2018. These assumptions are documented in the report titled "Kentucky Retirement Systems 2018 Actuarial Experience Study for the Period Ending June 30, 2018. The Total Pension liability as of June 30, 2020, was determined using these updated assumptions.

House Bill 1 passed during the 2019 Special Legislative Session allows certain employers in the KERS Non-hazardous plan to elect to cease participating in the System as of June 30, 2020 under different provisions that were previously established. Senate Bill 249 passed during the 2020 legislative session delayed the effective date of cessation for these provisions to June 30, 2021. Since each employer's elections are unknown at this time, no adjustment to the Total Pension Liability was made to reflect this legislation.

Senate Bill 249 passed during the 2020 legislative session and changed the funding period for the amortization of the unfunded liability to 30 years as of June 30, 2019. Gains and losses incurring in future years will be amortized over separate 20-year amortization bases. This change does not impact the calculation of the Total Pension Liability and only impacts the calculation of the contribution rates that would be payable starting July 1, 2020. There were no other material plan provision changes.

House Bill 8 passed during the 2021 regular session and changed the KERS nonhazardous actuarially accrued liability contribution (unfunded liability payment) that is payable by employers on or after July 1, 2021, from a value that is paid as a percent of pay on each employee to a set dollar amount and provide that the set dollar amount shall be allocated to each individual employer based upon the employer's percent share of the liability as of the June 30, 2019, actuarial valuation and shall be paid by employers in equal installments monthly.



# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

<b>Actuarial Assumptions</b>	
<b>Actuarial Valuation Date</b>	June 30, 2019
<b>Actuarial Cost Method</b>	Entry age normal
<b>Amortization Method</b>	Level percent of pay
<b>Asset Valuation Method</b>	20% of the difference between the market value of assets and the expected actuarial value of the assets is recognized.
<b>Remaining Amortization Period</b>	24 years, closed
<b>Actuarial Assumptions:</b>	
<b>Investment Rate of Return</b>	6.25%
<b>Inflation Rate</b>	2.30%
<b>Projected Salary Increases</b>	3.30% to 15.30%, varies by service
<b>Mortality Tables:</b>	
<b>Active Members</b>	Pub-2010 General Mortality tables projected with the ultimate rates from the MP-2014 mortality improvement scale using a base year of 2010.
<b>Healthy Retired Members</b>	System-specific mortality table based on mortality experience from 2013-2018, projected with the ultimate rates from MP-2014 mortality improvement scale using a base year of 2020.
<b>Disabled Members</b>	PUB-2010 Disabled Mortality Table, with a 4-year set-forward for both male and female rates, projected with the ultimate rates from the MP-2014 mortality improvement scale using a base year of 2010.
<b>Date of Experience Study</b>	The period July 1, 2014 - June 30, 2018
<b>Update Procedures Applied</b>	The actuarial valuation date of June 30, 2019, was rolled forward from the valuation date to the plan's fiscal year end of June 30, 2020 using standard roll forward procedures.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

For the year ended June 30, 2021, the Funding Commission recognized pension expense of \$797,828 and deferred outflows and deferred inflows related to the pension from the following sources:

	Deferred Outflows	Deferred Inflows
Difference between expected and actual experience	\$ 41,764	\$ -0-
Net difference between projected and actual earnings on investments	7,560	-0-
Change of assumption	82,816	-0-
Changes in proportion and difference between employer contributions and proportionate share of contributions	203,343	144,462
Contributions subsequent to the measurement date	558,073	-0-
<b>Total</b>	<b>\$ 893,556</b>	<b>\$ 144,462</b>

The \$558,073 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability during the year ended June 30, 2022. Other amounts reported as deferred outflows of resources and deferred inflows of resources will be recognized over a period of either five years for investment-related deferrals or the estimated remaining service life for active participants in the pension plan for other deferred items. As of June 30, 2020 plan year, the estimated remaining service life was 2.26 years. Other amounts reported as deferred outflows and deferred inflows of resources related to the pension will be recognized in pension expense as follows:

Deferred Amounts to be recognized in Fiscal Years  
Following the Reporting Date

Fiscal Years	
2022	\$ 198,797
2023	(20,920)
2024	6,360
2025	6,784
Total	\$ 191,021

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years for KERS. The most recent analysis, performed was for the period covering fiscal years 2014 through 2018, and is outlined in a report dated April 12, 2019. Several factors are considered in evaluating the long-term rate of return. Assumptions including long-term historical data, estimates inherent in current market data, and a log – normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected return, net of investment expense and inflation) were developed by the investment consultant for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and then adding expected inflation. The capital market assumptions developed by the investment consultant are intended for use over a 10-year horizon and may not be useful in setting the long-term rate of return for funding pension plans which cover a longer timeframe. The assumption is intended to be a long-term assumption and is not expected to change absent a significant change in the asset allocation, a change in the inflation assumption, or a fundamental change in the market that alters expected returns in future years.

The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the following table:

<b>Kentucky Retirement Systems</b>		
<b>Asset Class</b>	<b>Target Allocation</b>	<b>Long-Term Nominal Rate of Return</b>
Growth:		
US Equity	15.75%	4.30%
Non-US Equity	15.75%	5.25%
Private Equity	7.00%	5.15%
Specialty Credit/High Yield	15.00%	3.90%
Liquidity:		
Core Bonds	20.50%	-0.25%
Cash	3.00%	-0.75%
Diversifying Strategies:		
Real Estate	5.00%	5.30%
Opportunistic	3.00%	2.25%
Real Return	15.00%	3.95%
Total	100.00%	

The projection of cash flows used to determine the discount rate of 5.25% assumes that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 24-year amortization period of the unfunded actuarial accrued liability. The actuarial determined contribution rate is adjusted to reflect the phase in of anticipated gains on actuarial value of assets over the first four years of the projection period.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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June 30, 2020 is the actuarial valuation date upon which the total pension liability is based. The discount rate is defined as the single rate of return that when applied to all projected payments results in an actuarial value of projected benefits payments. A municipal bond rate was not used.

The following presents the net pension liability of the Funding Commission, calculated using the discount rate of 5.25%, as well as what the Funding Commission's net position liability would be if it were calculated using a discount rate that is one percentage point lower (4.25%) or one percentage point higher (6.25%):

	1% Decrease (4.25%)	Discount (5.25%)	1% Increase (6.25%)
The Commission's proportionate share	\$ 8,420,278	\$ 7,351,597	\$ 6,473,343

Detailed information about the KERS's fiduciary net position is available in the separately issued Kentucky Employees' Retirement System's Annual Financial Report (which is a matter of public record). The Commonwealth's Comprehensive Annual Financial Report should be referred to for additional disclosures related to KERS. The Kentucky Retirement System also issues a publically available financial report that includes financial statements and required supplementary information for the KERS. The report may be obtained online at [www.kyret.ky.gov](http://www.kyret.ky.gov).

In addition to the above defined benefit pension plan, the Funding Commission's employees are also eligible to participate in two deferred compensation plans sponsored by the Commonwealth. These plans are organized as a Section 457 plan and as a Section 401(k) plan under the Internal Revenue Code. Both plans permit employees to defer a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, or financial hardship. The Kentucky Public Employees Deferred Compensation Authority (KPEDCA) issues a publicly available financial report that includes financial statements and required supplementary information for the KPEDCA. The report may be obtained by writing to the Kentucky Public Employees Deferred Compensation Authority, 101 Sea Hero Road, Suite 110, Frankfort, Kentucky 40601-8862.

### **8. POST-EMPLOYMENT HEALTH CARE BENEFITS**

All regular full-time employees who work in non-hazardous duty positions of any state department, board, agency, county, city, school board, and any eligible local agencies participate in an Other Post-employment Benefit (OPEB) plan administered by the Kentucky Employees Retirement System (KERS), a cost-sharing multi-employer public employee retirement system. The plan provides health insurance benefits to plan members and also to certain beneficiaries of plan members under prescribed circumstances.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

**Covered Employees:** Contribution rates for employers and employees are established by Kentucky Statute KRS 21.427. The Traditional plan members do not contribute to the OPEB directly. Instead, assets have been allocated between the pension and the retiree medical liabilities on the basis of accrued liability as of July 1, 2020. This amount has been brought forward from that date based on actual cash flows and prorated allocation of investment returns. The hybrid plan member contributes 1% of his or her salary. Employer contributions are determined by the budget bill.

<b>Benefit Factor:</b>	Participation prior to July 2003		Participation between July 2003 and August 2008		Participation on or after September 2008	
	Months of Service	Percent of premium	Months of Service	Percent of premium	Months of Service	Percent of premium
	<48	0%	Greater than or equal to 120	\$10 per month for each year of service without regard to a maximum dollar adjusted by 1.5% annually.	Greater than or equal to 180	\$10 per month for each year of service without regard to a maximum dollar adjusted by 1.5% annually.
	48 to 119 inclusive	25%				
	120 to 179 inclusive	50%				
	180 to 239 inclusive	75%				
	240 or more	100%				

**Cost of Living**

**Adjustment (COLA):** Members participating after 2008 receive 1.5% increase annually.

Benefits and contribution rates are established by state statute. Per Kentucky Revised Statute 61.565, contribution requirements of active employees and participating organizations are established and may be amended by the Kentucky Retirement System's board. Employees with a participation date after 9/1/2008 were required to contribute an additional 1 percent of their salary for retiree healthcare benefits. The Funding Commission was contractually required to contribute 11.15 percent of covered payroll to the nonhazardous KERS insurance plan. Actuarially determined as an amount that, when combined with employee contributions, is expected to finance the cost and benefits earned by employee during the year, with an additional amount to finance any unfunded accrued liability. The Funding Commission's total statutorily required contributions to the KERS nonhazardous insurance plan for the year ended June 30, 2021 were \$84,914.

At June 30, 2021, the Funding Commission reported a liability of \$1,317,719 or its proportionate share of the collective net OPEB liability. The collective net OPEB liability was measured as of June 30, 2020, and the total OPEB liability used to calculate the net collective OPEB liability was determined by an actuarial valuation performed as of June 30, 2019, rolled forward to 2020 using generally accepted actuarial principles. The Funding Commission's proportion of the net OPEB liability was based on contributions to the OPEB plan relative to the total contributions of all participating entities, actuarially determined. At June 30, 2021, the Funding Commission's proportion was .051901 percent.

For the year ended June 30, 2021, the Funding Commission recognized OPEB expense of \$140,561 and deferred outflows and deferred inflows related to OPEB from the following sources:

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

	Deferred Outflows	Deferred Inflows
Difference between expected and actual experience	\$ 109,064	\$ 130,860
Net difference between projected and actual earnings on investments	18,395	-0-
Change of assumption	96,450	2,290
Changes in proportion and difference between employer contributions and proportionate share of contributions	90,276	58,527
Contributions subsequent to the measurement date	104,747	-0-
<b>Total</b>	<b>\$ 418,932</b>	<b>\$ 191,677</b>

Of the total amount reported as deferred outflows of resources related to OPEB, \$84,914 resulting from the Funding Commission's statutorily required contributions and \$19,833 resulting from the implicit subsidy subsequent to the measurement date and before the end of the fiscal year will be included as a reduction of the collective net OPEB liability during the year ended June 30, 2022. Other amounts reported as deferred outflows of resources and deferred inflows of resources will be recognized over a period of either five years for investment-related deferrals or the estimated remaining service life for active participants in the pension plan for other deferred items. As of June 30, 2020 plan year, the estimated remaining service life was 3.69 years. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in the Funding Commission's OPEB expense as follows:

Deferred Amounts to be recognized in Fiscal Years Following the Reporting Date	
Fiscal Years	
2022	\$ 56,763
2023	20,155
2024	40,179
2025	5,411
Total	\$ 122,508

*Actuarial assumptions:* The total OPEB liability, net OPEB liability, and sensitivity information shown in this report are based on an actuarial valuation performed as of June 30, 2019. The total OPEB liability

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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was rolled forward from the valuation date to the measurement date at June 30, 2020, using generally accepted actuarial principles.

<b>Actuarial Assumptions</b>	
<b>Actuarial Valuation Date</b>	June 30, 2019
<b>Experience Study</b>	The period July 1, 2008 - June 30, 2013
<b>Actuarial Cost Method</b>	Entry age normal, level percentage of pay
<b>Asset Valuation Method</b>	5 years smoothing
<b>Remaining Amortization Period</b>	24 years, closed
<b>Actuarial Assumptions:</b>	
<b>Investment Rate of Return</b>	6.25%
<b>Inflation Rate</b>	2.3%
<b>Payroll Growth Rate</b>	0%
<b>Salary Growth Rate</b>	3.30% to 15.30%, varies by service
<b>Mortality Tables:</b>	PUB-2010 General Mortality table projected with the ultimate rates from the MP-2014 mortality improvement scale using a base year of 2010.
<b>Healthcare Trend Rates (pre-65):</b>	Initial trend starting at 6.40% at January 1, 2022 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 14 years.
<b>Healthcare Trend Rates (post-65):</b>	Initial trend starting at 2.90% at January 1, 2022 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 14 years.
<b>Update Procedures Applied</b>	The actuarial valuation date of June 30, 2019, was rolled forward from the valuation date to the plan's fiscal year end of June 30, 2020 using standard roll forward procedures.

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# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

The long-term expected rate of return was determined by using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each asset class. The ranges are combined by weighting the expected future real rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the below table.

<b>Kentucky Retirement Systems</b>		
<b>Asset Class</b>	<b>Target Allocation</b>	<b>Long-Term Nominal Rate of Return</b>
Growth:		
US Equity	18.75%	4.50%
Non-US Equity	18.75%	5.25%
Private Equity	10.00%	6.65%
Specialty Credit/High Yield	15.00%	3.90%
Liquidity:		
Core Bonds	13.50%	-0.25%
Cash	1.00%	-0.75%
Diversifying Strategies:		
Real Estate	5.00%	5.30%
Opportunistic	3.00%	2.25%
Real Return	15.00%	3.95%
Total	100.00%	

The projection of cash flows used to determine the discount rate of 5.43 percent for the KERS Nonhazardous insurance plan assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 24 years (closed) amortization period of the unfunded actuarial accrued liability. The discount rate determination used an expected rate of return of 6.25% and a municipal bond rate of 2.45%, as reported in Fidelity Index's "20-Year Municipal GO AA Index" as of June 30, 2020. Based on the stated assumptions and the projection of cash flows as of each fiscal year ending, the plan's fiduciary net position and future contributions were projected to be sufficient to finance the future benefit payments of the current plan members. Therefore, the long-term expected rate of return on insurance plan investments was applied to all periods of the projected benefit payments paid from the retirement system. However, the cost associated with the implicit employer subsidy is not currently being included in the calculation of the KERS's actuarially determined contributions, and it is our understanding that any cost associated with the implicit subsidy will not be paid out of the KERS's trust. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy. The projection of cash used to determine the single discount rate assumes that the funds receive the required employer contributions each future year, as determined by the current funding policy established in statute. The



# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the Commonwealth's ACFR.

The projection of cash flows used to determine the single discount rate must include an assumption regarding future employer contributions made each year. The future contributions are projected in accordance with the current funding policy, as most recently revised by Senate Bill 249, passed during the 2020 legislative session. If there is a pattern of legislation that has a resulting effect of employers making contributions less than the actuarially determined rate, Gabriel Roeder Smith (GRS) may be required to project contributions that are reflective of recent actual contribution efforts regardless of the stated funding policy (as required by paragraph 50 of GASB Statement No. 74) legislation has been enacted for multiple years (for Fiscal Year 18/19, Fiscal Year 19/20, and Fiscal Year 20/21) that allowed certain employers (referred to as "Quasi" agencies) in the KERS Nonhazardous Fund to contribute 8.41% of pay into the insurance fund, which is less than the actuarially determined contribution rate. GRS confirmed that the single discount rate used in the GASB calculations remains unchanged if these Quasi agencies were assumed to continue making contributions at a reduced rate in future years.

*Sensitivity of the Funding Commission's proportionate share of the collective net OPEB liability to changes in the discount rate.* The following presents the Funding Commission's proportionate share of the collective net OPEB liability, as well as what the Funding Commission's proportionate share of the collective net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.43 percent) or 1-percentage-point higher (6.43 percent) than the current discount rate:

	1% Decrease (4.43%)	Discount (5.43%)	1% Increase (6.43%)
The Commission's proportionate share	\$ 1,570,578	\$ 1,317,719	\$ 1,110,173

*Sensitivity of the Funding Commission's proportionate share of the collective net OPEB liability to changes in the healthcare cost trend rates.* The following presents the Funding Commission's proportionate share of the collective net OPEB liability, as well as what the Funding Commission's proportionate share of the collective net OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower or 1 percentage-point higher than the current healthcare cost trend rates (Pre-65 - Initial trend starting at 6.40 percent at January 1, 2022, and gradually decreasing to 4.05 percent over a period of 14 years and Post-65 - Initial trend starting at 2.90 percent at January 1, 2022, and gradually decreasing to 4.05 percent over a period of 14 years ):

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

	1% Decrease	Current Healthcare Cost Trend Rate	1% Increase
The Commission's proportionate share	\$ 1,109,080	\$ 1,317,719	\$ 1,570,431

Detailed information about the KERS's fiduciary net position is available in the separately issued Kentucky Employees' Retirement System's Annual Financial Report (which is a matter of public record). The Commonwealth's Comprehensive Annual Financial Report should be referred to for additional disclosures related to KERS.

### 9. RISK MANAGEMENT

The Funding Commission is exposed to various risks of loss related to torts; theft of, damages to, and destruction of assets; and errors and omissions. The Funding Commission utilizes the Commonwealth's Risk Management Fund to cover exposure to these potential losses. The Commonwealth's Comprehensive Annual Financial Report should be referred to for additional disclosure related to the Risk Management Fund. The Funding Commission also purchases a commercial insurance policy for Directors and Officers insurance.

### 10. RELATED PARTY TRANSACTIONS

The Funding Commission received services from the Commonwealth Office for Technology (COT) which provides technical support for State government agencies in the application of information technology including major information resource functions such as data center operations, data and voice communications, data administration, hardware selection and installation, printing, and related end-user and customer support services. During 2021, the Funding Commission paid \$57,802 to COT for services provided.

The Funding Commission received assessments from the Commonwealth's Personnel Cabinet and Transportation Cabinet. During 2021, the Funding Commission received \$1,165,697 and \$240,634 from the Commonwealth's Personnel Cabinet and Transportation Cabinet, respectively, in assessments on workers compensation premiums. At June 30, 2021, assessments receivable from the Transportation Cabinet was \$57,099.

In October 2019, the Funding Commission purchased a corporate bond issued by State Street Corporation for \$1,505,000. State Street Corporation is the custodian of the Funding Commission's investments. The fair value of this bond was \$1,602,283 at June 30, 2021.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### 11. FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides 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) and the lowest priority to unobservable inputs (level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Funding Commission has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If asset or liability has a specified (contractual) term, the level 2 inputs must be observable for substantially the full term of the asset or liability.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurements.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

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

- *Fixed Income Investments*: Valued using pricing models maximizing the use of observable inputs for similar securities.

The following table sets forth by level within the hierarchy, the Special Fund's assets and liabilities measured at fair value on a recurring basis as of June 30, 2021 as follows:

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2021

<b>Assets at Fair Value as of June 30, 2021</b>				
	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
Investments:				
Corporate Bonds	\$ -0-	\$ 167,425,851	\$ -0-	\$ 167,425,851
U.S. Treasury Notes and Bonds	-0-	67,429,043	-0-	67,429,043
Taxable Municipals	-0-	40,431,763	-0-	40,431,763
U.S. Agency Mortgage-Backed Securities	-0-	23,045,328	-0-	23,045,328
Asset Backed Securities	-0-	16,645,113	-0-	16,645,113
Collateralized Mortgage Obligations	-0-	11,437,126	-0-	11,437,126
Collateralized Mortgage-Backed Securities	-0-	5,243,673	-0-	5,243,673
Investment in state pool	751,676	-0-	-0-	751,676
Local government	-0-	329,869	-0-	329,869
Total investments at fair value	\$ 751,676	\$ 331,987,766	\$ -0-	\$ 332,739,442

The following table sets forth by level within the hierarchy, the CWPF's assets and liabilities measured at fair value on a recurring basis as of June 30, 2021 as follows:

<b>Assets at Fair Value as of June 30, 2021</b>				
	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
Investments:				
Investment in state pool	\$ 267,195	\$ -0-	\$ -0-	\$ 267,195
Total investments at fair value	\$ 267,195	\$ -0-	\$ -0-	\$ 267,195

The following table sets forth by level within the hierarchy, the Self-Insurance Fund's assets and liabilities measured at fair value on a recurring basis as of June 30, 2021 as follows:

<b>Assets at Fair Value as of June 30, 2021</b>				
	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
Investments:				
Investment in state pool	\$ 894,785	\$ -0-	\$ -0-	\$ 894,785
Total investments at fair value	\$ 894,785	\$ -0-	\$ -0-	\$ 894,785

The Funding Commission's policy is to recognize transfers between levels as of the actual date of the event or changes in circumstances. There were no transfers between levels during the year ended June 30, 2021.

The Funding Commission holds investments which are exposed to various risks such as interest rate, market, and credit. Due to the level of risk associated with these securities and the level of uncertainty related to changes in value, it is at least reasonably possible that changes in various risk factors will occur in the near term that could materially affect the amounts reported in the accompanying financial statements.

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2021

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### 12. CONTINGENCIES

The Funding Commission is a plaintiff in a lawsuit regarding a penalty assessment for the audit period of 2013-2014 and assessments previously paid to the Funding Commission of approximately \$739,000. The Kentucky Office of Claims and Appeals ruled in favor of the defendant and ordered the Funding Commission to refund the amount in protest that was previously paid and an additional refund of about \$41,000 in coal assessments. The Funding Commission has sought judicial review of the Office of Claims and Appeals' decision in the Franklin Circuit Court. The Franklin Circuit Court has yet to rule on this matter.

On March 11, 2020, the World Health Organization declared Coronavirus (COVID-19) a pandemic. The continued spread of COVID-19, or any similar outbreaks in the future, may adversely impact the local, regional, national and global economies. The extent to which COVID-19 impacts the Funding Commission's operating results is dependent on the breadth and duration of the pandemic and could be affected by other factors management is currently not able to predict. One potential impact includes, but is not limited to, the potential negative impact to the workers' compensation insurance market. Accordingly, assessments levied on such workers' compensation premiums may be subject to further decline over the next twelve months. Management believes the Funding Commission is taking appropriate actions to respond to the pandemic; however, the full impact is unknown and cannot be reasonably estimated at the date the financial statements were available for issuance.

### 13. RECENT GASB PRONOUNCEMENT

Management has not currently determined what, if any, effects of implementation of the following statement may have on the financial statements:

**GASB Statement No. 87, *Leases***, will be effective for periods beginning after June 15, 2021. This statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources.

REQUIRED SUPPLEMENTARY INFORMATION

## KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

### SCHEDULE OF PROPORTIONATE SHARE OF THE NET PENSION LIABILITY

	2021	2020	2019	2018	2017	2016	2015
Proportion of the net pension liability (asset)	0.051901%	0.054045%	0.047471%	0.049631%	0.051054%	0.058366%	0.056081%
Proportionate share of the net pension liability	\$7,351,597	\$7,632,777	\$6,457,848	\$6,644,765	\$5,819,930	\$5,855,212	\$5,031,286
Covered payroll	\$ 739,993	\$ 790,512	\$ 725,032	\$ 767,371	\$ 825,402	\$ 946,984	\$ 962,246
Proportionate share of the net pension liability (asset) as a percentage of its covered payroll	993.47%	965.55%	890.70%	865.91%	705.10%	618.30%	522.87%
Plan fiduciary net position as a percentage of the total pension liability	14.01%	13.66%	12.84%	13.32%	14.80%	18.83%	22.32%

\*Note: This schedule is intended to present 10 years of the proportionate share of the net pension liability. Currently, only those years with information available are presented. The amounts presented above for the fiscal year were determined as of June 30 for the year prior (measurement date).

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## SCHEDULE OF PENSION CONTRIBUTIONS

	2021	2020	2019	2018	2017	2016	2015	2014
Statutorily required contribution	\$ 558,073	\$ 525,617	\$ 561,501	\$ 297,698	\$ 308,790	\$ 254,554	\$ 292,050	\$ 166,468
Contribution in relation to the statutorily required contribution	558,073	525,617	561,501	297,698	308,790	254,554	292,050	166,468
Contribution deficiency (excess)	\$ -0-	\$ -0-	\$ -0-	\$ -0-	\$ -0-	\$ -0-	\$ -0-	\$ -0-
Covered payroll	\$ 761,562	\$ 739,993	\$ 790,512	\$ 725,032	\$ 767,371	\$ 825,402	\$ 946,984	\$ 962,246
Contribution as a percentage of covered payroll	73.28%	71.03%	71.03%	41.06%	40.24%	30.84%	30.84%	17.30%
<b>Notes to Schedule</b>								
Valuation date	June 30, 2017	June 30, 2017	June 30, 2016	June 30, 2016	June 30, 2015	June 30, 2015	June 30, 2014	Not available
<b>Methods and assumptions used to determine contributions:</b>								
Actuarial cost method	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Not available
Experience study	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	Not available
Amortization method	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Not available
Asset valuation method	20% of the difference between market value of assets and the expected actuarial value of assets is recognized	20% of the difference between market value of assets and the expected actuarial value of assets is recognized	20% of the difference between market value of assets and the expected actuarial value of assets is recognized	20% of the difference between market value of assets and the expected actuarial value of assets is recognized	20% of the difference between market value of assets and the expected actuarial value of assets is recognized	Five-year smoothed market	Five-year smoothed market	Not available
Investment return	5.25%	5.25%	6.75%	6.75%	6.75%	7.50%	7.75%	Not available
Inflation	2.30%	2.30%	3.25%	3.25%	3.25%	3.25%	3.50%	Not available
Projected salary increase	3.55% to 15.55%, varies by service	3.55% to 15.55%, varies by service	4.0%, average	4.0%, average	4.0%, average, including inflation	4.0%, average, including inflation	4.50% per annum	Not available

**Mortality**

The rate of mortality for active members is based on the RP-2000 Combined Mortality Table projected to with scale BB to 2013 (multiplied by 50% for males and 30% for females). For health retired members and beneficiaries, the mortality table is the RP-2000 Combined Mortality Table projected with scale BB to 2013 (set back 1 year for females) For disabled members, the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set back 4 years for males) is used for the period after disability retirement. There is some margin in the current mortality tables for possible future future improvement in mortality rates and that margin will be reviewed again when the next experience investigation is conducted.

Note: This is a 10 year schedule. Years will be added to this schedule in future fiscal years until 10 years of information is available.

*See report of independent auditors.*



**KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION**

SCHEDULE OF PROPORTIONATE SHARE OF THE NET OPEB LIABILITY

	2021	2020	2019	2018	2017
Proportion of the net OPEB liability (asset)	0.051901%	0.054045%	0.047431%	0.049631%	0.051054%
Proportionate share of the net OPEB liability	\$1,317,719	\$1,201,364	\$1,124,547	\$1,258,623	\$1,065,238
Covered payroll	\$ 739,993	\$ 790,512	\$ 725,035	\$ 767,371	\$ 825,402
Proportionate share of the net OPEB liability (asset) as a percentage of its covered payroll	178.07%	151.97%	155.10%	164.02%	129.06%
Plan fiduciary net position as a percentage of the total OPEB liability	29.47%	30.92%	27.32%	24.37%	24.48%

\*Note: This schedule is intended to present 10 years of the proportionate share of the net OPEB liability. Currently, only those years with information available are presented. The amounts presented above for the fiscal year were determined as of June 30 for the year prior (measurement date).

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## SCHEDULE OF OPEB CONTRIBUTIONS

	2021	2020	2019	2018	2017	2016
Statutorily required contribution	\$ 84,914	\$ 91,759	\$ 98,024	\$ 60,975	\$ 64,075	\$ 65,454
Contribution in relation to the statutorily required contribution	84,914	91,759	98,024	60,975	64,075	65,454
Contribution deficiency (excess)	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>
Covered payroll	\$ 761,562	\$ 739,993	\$ 790,512	\$ 725,032	\$ 767,371	\$ 825,402
Contribution as a percentage of covered payroll	11.15%	12.40%	12.40%	8.41%	8.35%	7.93%

### Notes to Schedule

Valuation date	June 30, 2017	June 30, 2017	June 30, 2016	June 30, 2016	June 30, 2015	Not available
Experience Study	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013	

### Methods and assumptions used to determine contributions:

Actuarial cost method	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Not available
Amortization method	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Level percent of pay	Not available
Asset valuation method	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	Not available
Amortization period	26 Years, Closed	26 Years, Closed	27 Years, Closed	27 Years, Closed	28 Years, Closed	Not available
Investment return	6.25%	6.25%	7.50%	7.50%	7.50%	Not available
Inflation	2.30%	2.30%	3.25%	3.25%	3.25%	Not available
Payroll growth rate	0.00%	0.00%	4.00%	4.00%	4.00%	Not available
Projected salary increase	3.55% to 15.55%, varies by service	3.55% to 15.55%, varies by service	4.00% average	4.00% average	4.00% average	Not available
Healthcare Trend Rates (Pre-65)	Initial trend starting at 7.25% at 1/1/2019 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 13 years.	Initial trend starting at 7.25% at 1/1/2019 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 13 years.	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.	Not available
Healthcare Trend Rates (Post-65)	Initial trend starting at 5.10% at 1/1/2019 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 11 years.	Initial trend starting at 5.10% at 1/1/2019 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 11 years.	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 2 years.	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 2 years.	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 2 years.	Not available

### Mortality

RP-2000 Combined Mortality Table, projected to 2013 with Scale BB (set back 1 year for females)

Note: This is a 10 year schedule. Years will be added to this schedule in future fiscal years until 10 years of information is available.

*See report of independent auditors.*



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**REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE  
WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Directors  
Kentucky Workers' Compensation Funding Commission

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Kentucky Workers' Compensation Funding Commission (the Funding Commission), which comprise the statements of net position and fiduciary net position as of June 30, 2021, and the related statements of revenues, expenses, and changes in net position, changes in fiduciary net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 21, 2021.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Funding Commission's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Funding Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Funding Commission's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Funding Commission's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitation, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Funding Commission's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

#### Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Funding Commission's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Funding Commission's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Blue & Co., LLC*

Lexington, Kentucky  
September 21, 2021

# KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION

## SCHEDULE OF FINDINGS AND RESPONSES FOR THE YEAR ENDED JUNE 30, 2021

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### Summary of Auditor's Results

We have issued an unmodified opinion, dated September 21, 2021, on the financial statements of the Funding Commission as of and for the year ended June 30, 2021.

Our audit disclosed no instances of noncompliance which are material to the Funding Commission's financial statements.

Our audit disclosed no findings that are required to be reported in accordance with *Government Auditing Standards*.

### Findings Related to the Financial Statements

None noted.

**KENTUCKY WORKERS' COMPENSATION FUNDING COMMISSION**

SCHEDULE OF PRIOR YEAR FINDINGS AND THEIR RESPONSES  
FOR THE YEAR ENDED JUNE 30, 2021

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There were no findings reported for the year ended June 30, 2020.