

VLCT Unemployment Insurance Trust, Inc.

Audited Financial Statements
with Supplementary Information

*Years ended December 31, 2014 and 2013
with Report of Independent Auditors*

VLCT Unemployment Insurance Trust, Inc.

Audited Financial Statements
with Supplementary Information

Years ended December 31, 2014 and 2013

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Report of Independent Auditors

The Board of Directors
VLCT Unemployment Insurance Trust, Inc.

We have audited the accompanying financial statements of VLCT Unemployment Insurance Trust, Inc., which comprise the statements of net position as of December 31, 2014 and 2013, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of VLCT Unemployment Insurance Trust, Inc. as of December 31, 2014 and 2013 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters*Required Supplementary Information*

The accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis on pages 3 - 13 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 evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the VLCT Unemployment Insurance Trust, Inc.'s basic audited financial statements. The other information on page 25 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The other information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Emphasis of Matter

As more fully described in Note F, effective January 1, 2015, VLCT Unemployment Insurance Trust, Inc. merged with VLCT Health Trust, Inc. VLCT Health Trust, Inc. was the surviving entity and was subsequently renamed VLCT Employment Resource and Benefits Trust, Inc. All pre-merger services provided by VLCT Unemployment Trust, Inc. will continue uninterrupted through VLCT Employment Resource and Benefits Trust, Inc. Our opinion is not modified for this matter.

A handwritten signature in cursive script that reads "Johnson Lambert LLP". The signature is written in black ink and is positioned to the right of the main text block.

Burlington, Vermont
April 17, 2015

Vermont firm registration: 092-0000267

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis

Years ended December 31, 2014 and 2013

The management of VLCT Unemployment Insurance Trust, Inc. ("the Trust") presents the following overview and analysis of its financial operations for the fiscal year ended December 31, 2014, to be reviewed and considered in conjunction with the more detailed statements, schedules, exhibits and notes in the ensuing pages of this report.

Highlights

- Assets exceeded liabilities in 2014 by \$2,419,724, with an increase in total assets of \$162,470 (6.4%) and a decrease in liabilities of \$11,130 (3.9%). Assets exceeded liabilities in 2013 by \$2,246,124, with total assets increasing by \$294,554 (13.2%) and liabilities decreasing by \$8,371 (2.9%). Both increases were the result of operating surpluses with strong investment earnings strengthening total assets.
- Net position in 2014 increased by \$173,600 or 7.7% from 2013. This compares to an increase of \$302,925 or 15.6% experienced last year. The increase in 2014 was primarily due to strong investment earnings. To add to strong investment performance, the Trust produced an operating surplus in 2014 as claims were less than forecast. The increase in 2013 was primarily the result of an operating surplus that reflected lower than budgeted claim payments. Member contribution rates are set based on the worst case scenario (highest paid claims in one fund year that is included in funding analysis) to ensure that there will be enough funds to cover claim payments and yield a positive net position that will serve as a reserve during economic downturns or returned, in part, to the membership in the form of contribution credits.
- The ratio of net position to total assets increased from 88.8% in 2013 to 89.9% in 2014. This ratio measures the ability of the Trust to withstand both unanticipated increases in claims that are not offset by contributions and negative market performance during the year. The increase from 2013 to 2014 was due to a combination of conservative underwriting, an improved economy resulting in fewer claims, and strong investment earnings.
- The Trust returned \$400,000 in the form of rate credits to the members during the 2014 renewal. Rate credits of \$287,250 were returned to members in 2013. In 2014, the Board of Directors (the Board) approved rate credits of \$302,925 to be applied against 2015 contributions. This amount has been restricted in the statement of net position as of December 31, 2014.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Overview of the Trust's Financial Statements

The Trust's fiscal year is January 1 through December 31. All activities of the Trust are accounted for as an enterprise fund. The Trust's operations primarily include determination and collection of appropriate member contributions, issuance of claim benefit payments and payment of administrative costs of operating the Trust. Administrative costs include direct costs from operating the Trust, as well as indirect or fixed costs that are incurred by Vermont League of Cities and Towns (VLCT) and allocated to all three VLCT sponsored insurance trusts. Claims payments are made to claimants by the State of Vermont Department of Labor, with Equifax Corporation contracted to administer and report claims. The Trust reimburses the State of Vermont for these payments on a quarterly basis.

The annual financial report consists of three parts:

- Management's Discussion and Analysis
- Financial Statements and Disclosures
- Supplementary Schedule of Revenues and Expenses - Budgetary Basis

Management's discussion and analysis provides a narrative overview of the statements and comments on significant developments during the reporting period. The intention is to present a financial summary of operations for the past fiscal year and discuss the outlook for the ensuing year.

Required financial statements include:

- Statements of Net Position
- Statements of Revenues, Expenses and Changes in Net Position
- Statements of Cash Flows
- Notes to the Financial Statements

These statements present the Trust's status at December 31, 2014 and 2013 and financial developments during 2014 and 2013 for all activities. Comparative data for the prior year is included in the exhibits and notes to the financial statements.

The statements of net position present the economic position of the Trust as of December 31, 2014 and 2013, showing the assets owned by the Trust and how those assets are financed: by debt or short-term obligations, and by net position (the Trust's equity) or "surplus" as it is referred to in the insurance industry.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Overview of the Trust's Financial Statements- Continued

The statements of revenue, expenses and changes in net position show the operating transactions for the year, revenue and expenses. The result of operations is the change in net position. This figure added to last fiscal year's net position is the new net position total shown in both the statements of net position as well as the statements of revenue, expenses and changes in net position.

The statements of cash flows outline the cash flow resulting from operations, investment, and financing activities of the Trust.

Notes to the financial statements provide explanations of the accounting principles followed and of key items in the statements. They include tables showing detailed analysis of certain accounts. The supplementary schedule of revenues and expenses - budgetary basis for the year ended December 31, 2014 is presented for the purposes of additional analysis and is not a required part of the basic financial statements.

Please note that in the following analysis, when ratios are discussed, insurance terms are used along with the standard accounting terms. "Surplus" is used in the insurance industry for the accounting term "net position," and the terms may be used interchangeably in the following sections when discussing ratios.

Results and Analysis

The following table summarizes the statements of net position:

	<u>December 31, 2014</u>	<u>December 31, 2013</u>	<u>Percentage Change</u>	<u>December 31, 2012</u>	<u>Percentage Change</u>
Assets					
Cash and investments	\$ 2,621,711	\$ 2,448,942	7.1 %	\$ 2,212,566	10.7 %
Other assets	<u>69,797</u>	<u>80,096</u>	(12.9)%	<u>21,918</u>	265.4 %
Total assets	<u>\$ 2,691,508</u>	<u>\$ 2,529,038</u>	6.4 %	<u>\$ 2,234,484</u>	13.2 %
Liabilities					
	\$ 271,784	\$ 282,914	(3.9)%	\$ 291,285	(2.9)%
Net Position					
Restricted	302,925	400,000	(24.3)%	287,250	39.3 %
Unrestricted	<u>2,116,799</u>	<u>1,846,124</u>	14.7 %	<u>1,655,949</u>	11.5 %
Total net position	<u>2,419,724</u>	<u>2,246,124</u>	7.7	<u>1,943,199</u>	15.6
Total liabilities and net position	<u>\$ 2,691,508</u>	<u>\$ 2,529,038</u>	6.4 %	<u>\$ 2,234,484</u>	13.2 %

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

As of December 31, 2014, total assets increased by 6.4% from \$2,529,038 to \$2,691,508, compared to an increase of 13.2% from 2012 to 2013. Cash and cash equivalents decreased by \$742,761. In the second quarter \$800,000 of surplus funds were invested in the Trust's investment portfolio. A total of \$580,000 was invested in the fixed income portion of the portfolio, and \$280,000 was invested in the equity portion of the portfolio per the Trust's asset allocation policy. The Trust's investment portfolio grew by \$915,530. This was due to the aforementioned infusion of cash, plus investment earnings. Growth in the investment portfolio more than offset the decrease in cash and cash equivalents.

The investment portfolio returned 6.8% in 2014 compared to 5.7% in 2013. Fixed income outperformed its benchmark by .18%, and equities outperformed its benchmark by .58%.

As of December 31, 2014, total current liabilities decreased by 3.9% from \$282,914 to \$271,784 compared with a decrease of 2.9% from 2012 to 2013. In 2014 the decrease was due to lower claim liabilities, which was partially offset by an increase in unearned income. Unearned income increased because a lower surplus amount was approved to be returned to members in the form of contribution credits for the 2015 renewal year, thus more contributions were received prior to the beginning of the 2015 fiscal year than for 2014. The receipts for contributions paid in advance will not be recognized as revenue until 2015 and are therefore classified as a liability (unearned income) as of December 31, 2014. Conversely the drop in liabilities for 2013 was the result of a drop in unearned income, due to the large amount of contribution credits (\$400,000) that had been approved for 2014 renewal.

Net position increased in 2014 by 7.7% or \$173,600 from 2013. This compares to an increase of \$302,925 or 15.6% in 2013 from 2012. Operations in 2014 produced a modest operating income, as almost the entire underwriting surplus was returned to members in the form of contribution credits. However, strong return on the Trust's portfolio of \$144,200 largely explains the increase in net position. In 2013, claims were under budget by \$497,002. This was reduced by contribution credits of \$287,250. After accounting for general and administrative expenses that were under budget, this led to an operating surplus of \$228,873.

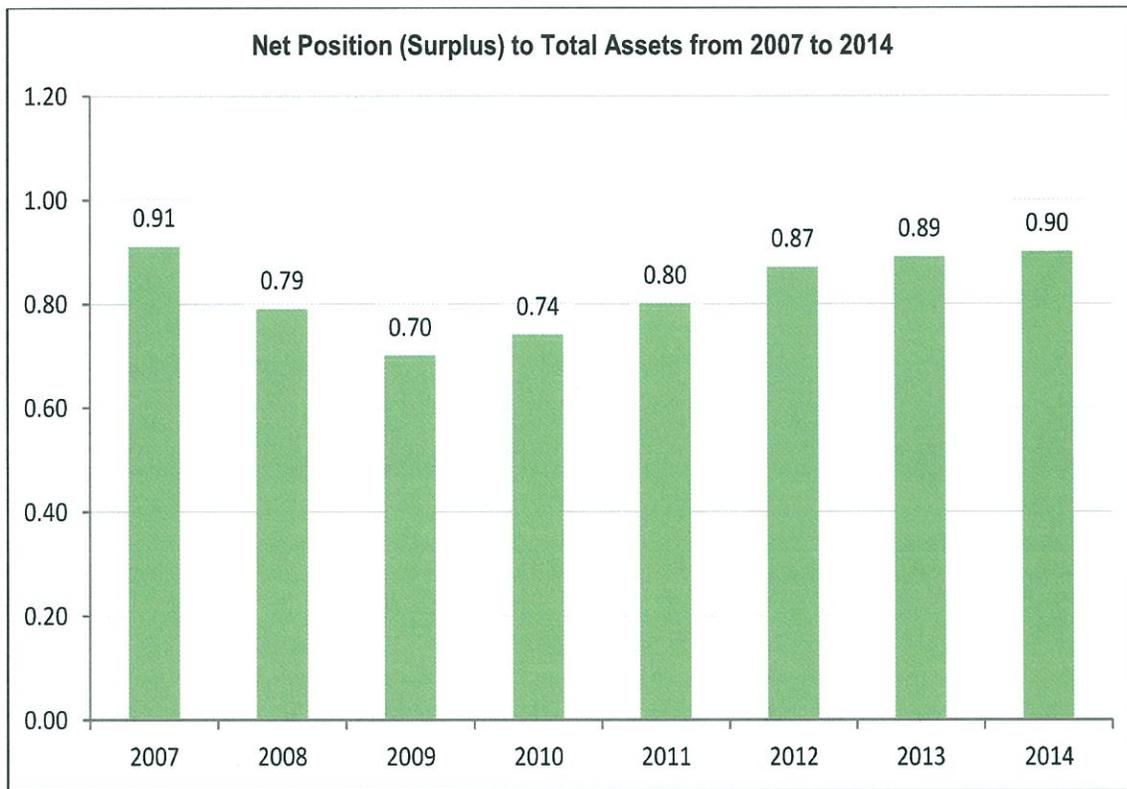
As can be seen in the following chart, net position or surplus as a ratio to total assets has been impacted by the recent recession. A higher ratio is preferable because it provides more of a cushion against unexpected losses, poor investment returns, or revenue shortfalls from insufficient contributions to cover benefit payments. In addition, benefit amounts or benefit duration changes that occur as a result of legislative actions could significantly impact this ratio.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

Because the Trust is fully self-insured and has no reinsurance to fall back on, a positive net position amount is particularly important for financial stability as shown by the trend leading up to the 2008 recession in the chart below. Though the Trust's ratio was over 90% in 2007, the large increase in claims combined with lower investment income resulting from the economic downturn depleted the Trust's net position significantly. Without that "reserve" from a substantial net position, the resulting hit on the Trust could have been catastrophic, resulting in some very significant rate increases to recoup the losses. With strong operating and investment performance between 2011 and 2014, the Trust has made some significant gains in getting back to that position of strength, moving much closer to the pre-recession levels.



VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

The following table summarizes the statements of revenues, expenses and changes in net position:

	December 31, 2014	December 31, 2013	Percentage Change	December 31, 2012	Percentage Change
Operating Revenues					
Fund contributions	\$ 664,170	\$ 841,344	(21.1)%	\$ 1,052,436	(20.1)%
Management fees	<u>51,750</u>	<u>52,000</u>	(0.5)%	<u>52,243</u>	(0.5)%
Total operating revenues	715,920	893,344	(19.9)%	1,104,679	(19.1)%
Operating Expenses					
Claims benefit payments	433,869	486,298	(10.8)%	442,123	10.0 %
General and administrative expenses	<u>252,651</u>	<u>178,173</u>	41.8 %	<u>152,110</u>	17.1 %
Total operating expenses	<u>686,520</u>	<u>664,471</u>	3.3 %	<u>594,233</u>	11.8 %
Operating income	<u>29,400</u>	<u>228,873</u>	(87.2)%	<u>510,446</u>	(55.2)%
Non-Operating Revenues					
Investment income, net of fees	<u>144,200</u>	<u>74,052</u>	94.7 %	<u>112,746</u>	(34.3)%
Change in net position	173,600	302,925	(42.7)%	623,192	(51.4)%
Net Position, Beginning of Year	<u>2,246,124</u>	<u>1,943,199</u>	15.6 %	<u>1,320,007</u>	47.2 %
Net Position, End of Year	<u>\$ 2,419,724</u>	<u>\$ 2,246,124</u>	7.7 %	<u>\$ 1,943,199</u>	15.6 %

The Trust had an operating income of \$29,400 in 2014 compared with an operating income of \$228,873 for 2013 and \$510,446 in 2012. In 2014 claims came in \$466,454 less than forecast. This was matched by \$400,000 in contribution credits returned to members. Years 2012 and 2013 also saw claims below forecast. Conservative rate setting methodology in 2013 resulted in almost \$500,000 in underwriting surplus reduced by the member contribution credits of \$287,250. In 2012, contributions were also more than sufficient to fully cover claims and administrative expenses, improving operations. Post recession rate setting with the current methodology allows for a gradual replenishment of surplus to build sufficient reserves to withstand the next economic downturn.

Contributions (before contributions credits) for 2014 reflected a rate of 1.9% that was intended to cover 2014 projected claims based on a worst case scenario. The rate for 2012 and 2013 was 1.9% as well. The taxable wage base for years 2012-2014 was \$16,000.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

Claim benefit payments decreased by 10.8% from 2013 to 2014 compared to a 10.0% increase from 2012 to 2013. While the claim count increased in 2014, claim payments dropped. This is likely an indicator of an improving job market where unemployed people are able to find a new job faster than had been possible in the last few years. In addition, a smaller percentage of higher cost claims occurred in 2014 offset by a larger number of credits; there was a substantial shift from lack of work to subsequent employer claims which tend to be mostly part time workers that are less costly. Because the contribution estimates reflected rates that anticipated worst case benefit disbursements, these payments were under budget by \$466,454 or 51.8%.

General and administrative expenses for the year increased from 2013 by \$74,478 or 41.8%. The increase from last year is mainly attributable to three items: (1) \$30,794 for the HR consulting project. The HR consulting project also explains the budget overage on the following schedule. This item was approved by the Board to be funded from surplus and so was not included in the 2014 budget; (2) an increase in data services expense of \$24,189. The Trust purchased an Unemployment Insurance underwriting software program from David Corp that was implemented late in 2013. This year was the first year of full depreciation on the new software program; (3) an increase in the VLCT administrative costs of \$10,116 primarily due to a combination of the normal budgeted increase and a shift in direct costs attributable to the reduction in Health Trust operations.

Net investment earnings for 2014 were \$144,200 compared with net investment earnings of \$74,052 in 2013. Out of this total, there was a net market gain (net realized and net unrealized) of \$79,075 in 2014 compared with net gain of \$35,206 in 2013. The balance of the year to year change in net investment earnings for both years is in interest and dividends earned. The increase in earnings from 2013 to 2014 is attributable to better performance in the fixed income portfolio, as well as a larger asset base as a result the \$800,000 cash infusion mentioned previously.

The asset allocation at the end of 2014 is comprised of 34.4% equities, 62.4% fixed income, and 3.2% cash equivalents. This compares with 33.4% equities, 65.4% fixed income, and 1.2% cash equivalents at the end of 2013. Weighted returns at year end 2014 were 6.19% for the fixed income portfolio (compared with the Barclays Capital Aggregate market index of 6.01%), while the equity portfolio showed weighted returns of 10.04% (compared with the blended benchmark of 9.46%). Both equities and fixed income outperformed their respective benchmarks.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

The following table summarizes budgeted revenues and expenses versus actual results, showing the variance from budgeted for the year ended December 31, 2014:

	<u>Budget</u>	<u>Actual</u>	<u>Variance</u>
Operating Revenues			
Fund contributions	\$ 1,064,259	\$ 664,170	\$ (400,089)
Management fees	<u>51,750</u>	<u>51,750</u>	<u>-</u>
Total operating revenues	1,116,009	715,920	(400,089)
Operating Expenses			
Claims benefit payments	900,323	433,869	466,454
General and administrative expenses	<u>220,575</u>	<u>252,651</u>	<u>(32,076)</u>
Total operating expenses	<u>1,120,898</u>	<u>686,520</u>	<u>434,378</u>
Operating excess of revenues over expenditures	(4,889)	29,400	34,289
Non-operating - investment income (loss)	<u>(3,900)</u>	<u>144,200</u>	<u>148,100</u>
Excess of Revenues Over Expenditures	<u>\$ (8,789)</u>	<u>\$ 173,600</u>	<u>\$ 182,389</u>

As shown in this budget analysis, the operating surplus of \$29,400 significantly exceeded the budgeted operating loss of \$4,889. The variance in actual operating surplus to budget is attributable to the conservative rate-setting process, with estimated claim benefit payments based on worst case scenario as previously discussed.

To determine member contributions or premiums, the Trust has used a retrospective rate-setting approach, budgeting for the worst case and paying back to members the difference between the actual and budgeted amounts, along with any investment income earned on the surplus funds. Both the budget for the ensuing year and distributions from prior year claims activity are based on an actuarial rate study completed annually. Distributions of \$400,000 in the form of renewal rate credits were returned to members in 2014. A \$287,250 distribution was returned to members in 2013.

On the revenue side, contributions were under budget by \$400,089, a result of the rate credit that was approved for 2014. The budget is shown gross of that credit, which reduces prior year surplus.

Actual investment earnings (of which only investment fees are budgeted) produced net investment income of \$148,100 in excess of budget, increasing the overall variance over budget to \$182,389.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Results and Analysis - Continued

Claims benefit payments were budgeted based on a maximum benefit ratio calculated from trend data for the period 2001 to 2013 (with 2013 projected), and applied to the 2014 projected taxable wage base of \$58.2 million. Years 2009 through 2011 trended high with 2009 being the worst benefit payout year at a 1.49% benefit ratio (2010 and 2011 were 1.34% and 1.17%, respectively). The payout for 2012 and 2013 dropped to 0.77%.

Actual benefit payments for 2014 were 10.8% lower than in 2013. The first and second quarters were each 2% higher than the same period a year earlier. The third quarter was 28% below 2013 levels, while the fourth quarter was 27% below 2013 levels. In 2013, all quarters were higher than in 2012, with the exception of the first quarter, with claim payments ending the year 10.0% higher than the prior year.

General and administrative expenses were higher than budgeted primarily due to the cost of the HR consulting project.

Additional variances to note within the individual budgets for operating expenses include:

- Actuarial was below budget by \$2,803 or 35% due to less actuarial study hours billed by the actuary.
- Data Services was above budget by \$3,864 or 17.6% because a portion of the NavRisk implementation costs that were budgeted in 2013 were actually billed and paid in 2014. NavRisk was implemented towards the end of 2013.
- Insurance was below budget by \$886 or 44.3%. With the exception of E/O and D/O all insurance is now included in the VLCT administration charge.
- Board Travel/Training is below budget by \$1,420 or 47.3% due to less travel by Board members than anticipated.
- Miscellaneous is above budget by \$3,810. This item was used to account for expenses relating the UVM MPA intern. This was an expense approved by the Board to be spent from surplus, and so was therefore not included in the budget.
- HR consulting project for \$30,794. This line item was not included in the original budget and was approved by the Board mid-year.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Outlook and Economic Factors

Unemployment rates in Vermont continue to be well below 6%. The U.S. economic recovery continues and the Trust has benefited from this improvement. The Trust saw an 10.8 percent reduction in its claim charges over the past year. This continues a trend of stable or dropping claims which began in the second quarter of 2010.

As a result of continuing positive results, the Trust's rates for 2015 were renewed at a rate lower than the prior year.

The chart below illustrates the average rate and estimated taxable wages for the current and previous three years:

Year	Average Rate	Trust Taxable Wages*	Taxable Wage Base
2015	1.80%	\$58.8 million	\$16,400
2014	1.90%	\$58.2 million	\$16,000
2013	1.90%	\$57.8 million	\$16,000
2012	1.90%	\$57.4 million	\$16,000

The taxable wage base is the maximum amount used per employee, or their actual wages if below the maximum. The wage base is set by the State and had historically been \$8,000 for many years. Due to the impact of the 2009 recession on the State's unemployment insurance trust, the amount was increased to \$10,000 in 2010 and then increased two more times to \$13,000 in 2011 and to \$16,000 in 2012. The State increased the amount to \$16,400 in 2015.

The 2014 actuarial study projected a net gain for the Trust and recommended granting a contribution rate credit. The Board voted to provide a contribution rate credit for 2015 in the amount of \$302,925, which is a decrease over the 2014 contribution rate credit of \$400,000. Last year the Board also decided to set aside some funds for developmental startup costs for potential new business opportunities such as a human resources assistance program. This study was completed and discussions between the VLCT trusts and VLCT are ongoing to consider initiating a human resources assistance program in mid to late 2015. The Board also provided funding for a Risk Management Services intern from the University of Vermont. This is a pilot program to determine the viability of a public administration internship at VLCT.

Claims have remained relatively stable and are below their 2009-2010 highs. This should allow the Trust to continue to maintain a strong net position to meet its obligations going forward.

VLCT Unemployment Insurance Trust, Inc.

Management's Discussion and Analysis (Continued)

Outlook and Economic Factors - Continued

The Trust implemented a new underwriting management software system for the 2014 renewal. The implementation process went smoothly. The new system (NavRisk), purchased from the same company (David Corp.) that provides underwriting and claims administration software to VLCT PACIF, will lead to more accurate and efficient renewal underwriting and program administration. The 2015 renewal went smoothly using the NavRisk system.

The Trust and the VLCT Health Trust, Inc. Boards met throughout 2014 to discuss a merger of the two trusts, as well as new business opportunities. The proposed merger received unanimous approval of the board and membership of each trust. The merged entity, VLCT Employment Resource and Benefits Trust (VERB), began operations on January 1, 2015. VERB combines the assets, programs, and operations of the former Health and Unemployment Trusts. The current Board has eight members, all former Health and Unemployment Trust board members and a starting Net Position in excess of \$4 million.

Requests for Information

This financial report is designed to provide a general overview of VLCT Unemployment Insurance Trust, Inc.'s finances for all those with an interest in the Trust's finances. Questions concerning any of the information provided in this report or requests for financial information should be addressed to the Chief Financial Officer at the Vermont League of Cities and Towns, 89 Main Street, Suite 4, Montpelier, Vermont, 05602-2948, or by calling 802-229-9111.

VLCT Unemployment Insurance Trust, Inc.

Statements of Net Position

	As of December 31,	
	<u>2014</u>	<u>2013</u>
Assets		
Cash and cash equivalents	\$ 346,082	\$ 1,088,843
Debt securities, at fair value	1,469,099	900,083
Mutual funds, at fair value	806,530	460,016
Accrued investment income	11,205	7,477
Prepaid expenses	<u>58,592</u>	<u>72,619</u>
 Total Assets	 <u>\$ 2,691,508</u>	 <u>\$ 2,529,038</u>
 Liabilities and Net Position		
Liabilities		
Due to Vermont Department of Labor	\$ 95,160	\$ 130,117
Unearned income	160,511	139,000
Net due to VLCT	3,781	3,996
Accounts payable	<u>12,332</u>	<u>9,801</u>
Total liabilities	271,784	282,914
 Net Position		
Restricted	302,925	400,000
Unrestricted	<u>2,116,799</u>	<u>1,846,124</u>
Total net position	<u>2,419,724</u>	<u>2,246,124</u>
 Total Liabilities and Net Position	 <u>\$ 2,691,508</u>	 <u>\$ 2,529,038</u>

See accompanying notes to the financial statements.

VLCT Unemployment Insurance Trust, Inc.

Statements of Revenues, Expenses, and Changes in Net Position

	Years ended December 31,	
	2014	2013
Operating Revenues		
Member contributions	\$ 664,170	\$ 841,344
Management fees	51,750	52,000
Total operating revenues	715,920	893,344
Operating Expenses		
Claims benefit payments	433,869	486,298
General and administrative expenses	252,651	178,173
Total operating expenses	686,520	664,471
Net operating income	29,400	228,873
Non-Operating Revenues (Expenses)		
Investment income	69,428	42,315
Investment income - net realized gains and change in fair value	79,075	35,206
Investment management fees	(2,957)	(2,320)
Investment consulting fees	(1,346)	(1,149)
Net non-operating revenues	144,200	74,052
Change in Net Position	173,600	302,925
Net Position, Beginning of Year	2,246,124	1,943,199
Net Position, End of Year	\$ 2,419,724	\$ 2,246,124

See accompanying notes to the financial statements.

VLCT Unemployment Insurance Trust, Inc.

Statements of Cash Flows

	Years ended December 31,	
	2014	2013
Cash Flows from Operating Activities		
Receipts for member contributions	\$ 685,681	\$ 813,552
Receipts for management fees	51,750	52,000
Payments for claims	(468,826)	(469,339)
Payments for general and administrative expenses	(236,305)	(234,623)
Net cash provided by operating activities	32,300	161,590
 Cash Flows from Investing Activities		
Receipts of interest income	65,700	43,049
Investment management fees	(2,957)	(2,320)
Investment consulting fees	(1,346)	(1,149)
Purchases of investments	(2,710,539)	(1,135,187)
Proceeds of investments	1,874,081	1,082,069
Net cash used in investing activities	(775,061)	(13,538)
 Net Change in Cash and Cash Equivalents	(742,761)	148,052
 Cash and Cash Equivalents, Beginning of Year	1,088,843	940,791
 Cash and Cash Equivalents, End of Year	\$ 346,082	\$ 1,088,843
 Reconciliation of Operating Income to Net Cash Provided By Operating Activities		
Net operating income	\$ 29,400	\$ 228,873
Changes in assets and liabilities:		
Prepaid expenses	14,027	(69,784)
Due to/from VLCT	(215)	14,868
Due to Vermont Department of Labor	(34,957)	16,959
Unearned income	21,511	(27,792)
Accounts payable	2,534	(1,534)
 Net cash provided by operating activities	\$ 32,300	\$ 161,590

See accompanying notes to the financial statements.

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements

Years ended December 31, 2014 and 2013

Note A - Organization and Nature of Operations

Organization

VLCT Unemployment Insurance Trust, Inc. ("the Trust") was incorporated in 1978 to provide Vermont municipalities with a stable, cost effective means to maintain their unemployment costs at the lowest possible levels. Services performed by the Trust include (1) payment of costs due to unemployment claims filed against the municipality; (2) a professional claims management system to review and monitor all data and reports upon filing for unemployment compensation; (3) legal and administrative representation at hearings and appeals before the Vermont Department of Labor up through the Vermont Supreme Court; (4) information on current legislation and representation before the Vermont legislature on all unemployment matters affecting Vermont municipalities; (5) effective cost-control programs on all aspects of the unemployment compensation law and how it affects cities and towns; and (6) an affiliation with the Vermont League of Cities and Towns ("VLCT"), an organization dedicated to the betterment of Vermont local government.

The Trust had 210 and 211 members as of December 31, 2014 and 2013, respectively.

During 2015, the Trust has merged with VLCT Health Insurance Trust, Inc. as more fully described in Note F.

Note B - Summary of Significant Accounting Policies

Basis of Accounting

The financial statements of the Trust have been prepared using the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("GAAP") as applied to governmental entities. The Trust also follows all statements in accordance with Government Accounting Standards Board ("GASB"). The Trust uses the economic resources measurement focus and the accrual basis of accounting and is accounted for as a proprietary enterprise fund.

Risks and Uncertainties

The Trust's operating results and financial condition are affected by numerous factors and circumstances inherent within the insurance industry, some of which it can neither predict nor control. Among them are (1) the state of the economy and the associated unemployment levels which impact claims benefit payments; (2) fluctuations in interest rates affect the value and income yield of the Trust's investment portfolio in the short-term, and often affect default and prepayment rates over time; (3) legislation that might impact benefit payments or duration of benefits. Should any of these or similar events occur, the Trust's operating results and financial condition may be affected.

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note B - Summary of Significant Accounting Policies (Continued)

Subsequent Events

The Trust has evaluated subsequent events for disclosure and recognition through April 17, 2015, as more fully described in Note F, the date on which these financial statements were available to be issued.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

The Trust engages an independent actuary to estimate a target net position to protect against potential future financial losses. The Trust does not record a liability for future claims and claims handling expenses due to the nature of the contracted relationship between the Trust and its members, and the claims paid nature of the Participation and Indemnification Agreement ("the Agreement") signed by each member upon joining the Trust. The Trust is only responsible for the claims of its current members, as outlined by the Agreement. As more fully described in Note E, the target net position protects against potential financial losses in the event of inadequate rates charged to members due to unexpectedly high claims and/or negative investment income.

Due to Vermont Department of Labor

The Vermont Department of Labor pays claims benefits when incurred and is reimbursed by the Trust on a quarterly basis, a quarter in arrears. Claims benefits payable for claims incurred in the last quarter of December 31, 2014 and 2013 are classified as Due to Vermont Department of Labor on the statements of net position.

Debt Securities/Mutual Funds

The Trust accounts for its investments in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* ("Statement No. 31"). Statement No. 31 establishes fair value standards on accounting for all investments held by governmental external investment pools and governmental entities. All investment income, including changes in the fair value of investments, is recognized in the statements of revenues, expenses and changes in net position. Realized gains and losses are determined using the specific identification method for debt securities and the average cost method for mutual funds. The calculation of realized gains and losses is independent of the calculation of the net change in fair value of investments. Realized gains and losses on investments that had been held for more than one year and sold in the current year were included as a change in the fair value of investments reported in the prior years and the current year. Investment purchases are recognized on the trade date. Investments are stated at fair value based on quoted market prices or prices obtained from a recognized pricing service.

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note B - Summary of Significant Accounting Policies (Continued)

Cash and Cash Equivalents

The Trust's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date acquired by the Trust.

The Trust's carrying amount of cash deposits and the bank balance at December 31, 2014 and 2013 were as follows:

	December 31, 2014		December 31, 2013	
	Book	Bank	Book	Bank
	Balance	Balance	Balance	Balance
Insured/FDIC	\$ 250,000	\$ 250,000	\$ 250,000	\$ 250,000
Uninsured, Collateralized by US Gov't and Agency Securities held by the People's United Bank Trust Department with a security interest granted to the Trust	96,082	98,132	838,843	838,837
Total	\$ 346,082	\$ 348,132	\$ 1,088,843	\$ 1,088,837

The difference between the book balance and the bank balance is due to reconciling items such as deposits in transit and outstanding checks.

The Federal Depository Insurance Corporation ("FDIC") insures amounts on deposit up to the limits as prescribed by the law. The Trust holds funds with financial institutions in excess of the FDIC insured amount, however, the Trust has not experienced any losses in such accounts and does not believe it is exposed to any significant credit risk on cash and cash equivalents. The Trust's deposits with People's United Bank are fully collateralized.

Prepaid Expenses

Payments for errors & omissions and professional liability insurance and subscriptions relating to the unexpired portion of the insurance agreements and the unused portion of subscriptions, as well as payments for the unexpired portion of software and software-related service agreements, are recorded as prepaid expenses.

Member Contributions

The Trust bills member contributions based on the members' reported taxable payroll from prior periods limited to \$16,000 per employee multiplied by a rate established by the Board of Directors ("the Board"). Underwriting and rate-setting methods and policies are established and applied after consultation with an independent actuary.

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note B - Summary of Significant Accounting Policies (Continued)

Unearned Income

Unearned income represents the amounts billed and collected at December 31, 2014 and 2013 for member contributions with coverage effective dates of January 1, 2015 and January 1, 2014, respectively.

Income Taxes

The Trust is incorporated as a nonprofit corporation under the Vermont Nonprofit Corporation Act. The Trust's income is tax-exempt under Internal Revenue Code Section 115, which pertains to political subdivisions. Accordingly, the accompanying financial statements do not include a provision for federal or state income taxes.

Classification of Revenues and Expenses

The Trust reports itself as a business-type activity as defined in GASB 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. Business-type activities are financed in whole or in part by fees charged to external parties. Business-type activities distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses 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 Trust's enterprise fund include fund contributions and fees received from providing services. Operating expenses include claims paid and the costs of providing services and operating all programs. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Note C - Investments

The Trust's investment policy, as approved by the Board, contains certain provisions and limitations intended to mitigate the Trust's exposure to various investment risks, such as credit risk (including custodial risk and concentration risk) and interest rate risk, as follows:

- *Credit risk* - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit risk is measured by an assigned rating from a nationally recognized credit rating agency such as Standard and Poor's or Moody's Rating Services. These organizations look at a number of factors in order to evaluate the credit risk of an obligation and rate the risk. This rating allows investors to make informed buying and selling decisions. The Trust's investment policy is structured with limitations and guidelines intended to mitigate the components of credit risk as summarized in the following three bullet points.

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note C - Investments (Continued)

- *Concentration of credit risk* - Concentration risk is the risk of loss attributable to the magnitude of an investment in a single issuer (with the exception of U.S. Government Obligations, which have no limit) to 5% of total investments. There are no single investments other than U.S. Government Obligations that exceed the limit as of December 31, 2014 and 2013.
- *Custodial credit risk* - Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Trust will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Neither the Vermont Statutes nor the Trust's investment policy guidelines contain requirements limiting custodial credit risk other than indicating that "prudent investment policies" should be followed. An agreement with People's United Bank, the custodial financial institution for the investment portfolio, is in place and indemnifies the Trust against losses caused by negligence or dishonesty.
- *Interest rate risk* - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in interest rates. The Trust's investment policy limits the average effective duration to 8 years.

The following table provides a summary of the fair value of the Trust's investment portfolio by contractual maturity. The expected maturities in the following table may differ from the contractual maturities because certain borrowers may have the right to call or prepay obligations with or without penalty.

	December 31, 2014				
	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years	Total
U.S. Treasuries	\$ -	\$ 267,252	\$ 47,761	\$ 116,909	\$ 431,922
U.S. Agencies	-	-	-	64,249	64,249
U.S. Agency MBS	-	117,404	4,218	-	121,622
Corporate Bonds	13,018	298,243	255,225	255,342	821,828
Municipal Bonds	-	-	-	12,560	12,560
Foreign Bonds	-	10,494	-	6,424	16,918
Total	\$ 13,018	\$ 693,393	\$ 307,204	\$ 455,484	\$ 1,469,099

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note C - Investments (Continued)

The table below outlines the Standard and Poor's credit ratings of the Trust's investment holdings as of December 31, 2014:

	U.S. <u>Treasuries</u>	U.S. <u>Agencies</u>	U.S.Agency <u>MBS</u>	Corporate <u>Bonds</u>	Municipal <u>Bonds</u>	Foreign <u>Bonds</u>	<u>Total</u>
AAA	\$ 431,922	\$ -	\$ -	\$ 118,706	\$ -	\$ -	\$ 550,628
AA+	-	-	99,598	14,513	6,332	-	120,443
AA	-	-	-	26,060	-	-	26,060
AA-	-	-	-	16,423	6,228	10,494	33,145
A+	-	-	-	25,673	-	6,424	32,097
A	-	-	-	107,851	-	-	107,851
A-	-	-	-	127,012	-	-	127,012
BBB+	-	-	-	176,003	-	-	176,003
BBB	-	-	-	94,005	-	-	94,005
BBB-	-	-	-	38,373	-	-	38,373
Not Rated	-	64,249	22,024	77,209	-	-	163,482
Total	<u>\$ 431,922</u>	<u>\$ 64,249</u>	<u>\$ 121,622</u>	<u>\$ 821,828</u>	<u>\$ 12,560</u>	<u>\$ 16,918</u>	<u>\$ 1,469,099</u>

The effective duration is used to assess interest rate risk by estimating the sensitivity of fixed income securities to interest rate changes. The effective duration estimates the percentage change in the market value of an investment (or an investment portfolio) for a one percent change in interest rates. It makes assumptions regarding the most likely timing and amounts of variable cash flows for investments that are highly sensitive to interest rate changes, such as mortgage-backed securities, callable bonds, and variable-rate debt.

The following were the effective durations of investments held by the Trust as of December 31, 2014:

	<u>Fair Value</u>	<u>Effective Duration</u>
U.S. Treasuries	\$ 431,922	6.88
U.S. Agencies	64,249	3.80
U.S. Agency MBS	121,622	3.70
Corporate Bonds	821,828	7.50
Municipal Bonds	12,560	1.75
Foreign Bonds	16,918	10.50
Total	<u>\$ 1,469,099</u>	5.92

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note C - Investments (Continued)

The average effective duration of the investment portfolio as of December 31, 2014 and 2013, was 5.92 and 5.49 years, respectively.

The following table shows the classifications of the Fund's mutual fund investments as of December 31, 2014 and 2013:

Classification	2014 Fair Value	2013 Fair Value
Large Cap Blend	\$ 246,807	\$ 139,401
Large Cap Growth	-	-
Large Cap Value	249,720	137,428
Mid Cap Blend	82,036	48,206
Mid Cap Growth	-	-
Mid Cap Value	-	-
Small Cap Blend	77,994	49,054
High Yield	74,130	43,582
World Bond	75,843	42,345
Total	<u>\$ 806,530</u>	<u>\$ 460,016</u>

Net realized gains on the sale of investments were \$17,848 and net unrealized gains attributable to the change in fair value of investments were \$61,227 for the year ended December 31, 2014. Net realized gains on the sale of investments were \$50,829 and net unrealized losses attributable to the change in fair value of investments were \$15,623 for the year ended December 31, 2013.

Note D - Administrative Services Provided by VLCT

The accompanying financial statements represent the general operations of the Trust and do not include the operations and financial condition of VLCT or other affiliated organizations. VLCT provides staff, office space and equipment usage to the Trust. The following VLCT expenses are attributable to the Trust.

- Salary and benefits for administrative staff including finance, human resource, production and general administrative support
- Office costs including all building-related expenses and insurances
- Equipment and communications costs
- Printing and supplies
- Travel and training for administrative functions
- Non-Trust Officers costs
- Contracted services
- Dues and subscriptions for administrative staff

VLCT Unemployment Insurance Trust, Inc.

Notes to the Financial Statements (Continued)

Note D - Administrative Services Provided by VLCT (Continued)

- Services provided for administrative activities
- Miscellaneous costs related to administrative activities

For the years ended December 31, 2014 and 2013, expenses allocated to the Trust were \$118,760 and \$108,644, respectively. These costs are included as a component of general and administrative expenses on the statements of revenues, expenses and changes in net position. As of December 31, 2014 and 2013, VLCT owed the Trust \$3,781 and \$3,996, respectively.

Note E - Net Position

As discussed in Note B, the Trust does not record a liability for future claims due to the claims paid nature of unemployment insurance and the Agreement with its members. Therefore beginning in 2010, the Board decided to no longer declare a portion of net position as designated for future claims liabilities.

As of December 31, 2014, the Trust has established a target net position of \$1,351,839 based on an actuarial assessment of variability of net income. The target net position represents a 99.9% confidence level as of December 31, 2014. The purpose of the net position target is to protect against potential financial losses in the event of unexpected high claims and/or possible poor investment returns. The net position target will be adjusted each year to reflect the most recent financial results. As of December 31, 2013, the Trust established a target net position of \$1,493,951.

The Trust budgets on a retrospective basis, giving back to members known surpluses in order to reduce future rates based on an actuarial assessment. The Trust returned \$400,000 and \$287,250 of contribution credits to the members during the years ended December 31, 2014 and 2013, respectively. During 2014, the Board also approved \$302,925 of contribution credits to be allocated to individual members upon renewal in 2015. Contribution credits approved by the Board for distribution during the following renewal year are recorded as restricted on the statements of net position.

Note F - Subsequent Event

Effective January 1, 2015, and as approved by the respective board of directors, the Trust merged with VLCT Health Trust, Inc. VLCT Health Trust, Inc. is the surviving entity and was subsequently renamed VLCT Employment Resource and Benefits Trust, Inc. All pre-merger services provided by VLCT Health Trust, Inc. and the Trust will continue uninterrupted through VLCT Employment Resource and Benefits Trust, Inc. The VLCT Employment Resource and Benefits Trust, Inc. will succeed to all assets, liabilities and other obligations of VLCT Health Trust, Inc. and the Trust.

VLCT Unemployment Insurance Trust, Inc.

Schedule of Revenues and Expenses - Budgetary Basis

December 31, 2014

(Unaudited)

	Budget	Actual	Variance Favorable / (Unfavorable)
Revenues			
Contributions	\$ 1,064,259	\$ 664,170	\$ (400,089)
Management fees	51,750	51,750	-
Investment income - interest and dividends	-	69,428	69,428
Investment income - change in fair value	-	79,075	79,075
Total revenues	<u>1,116,009</u>	<u>864,423</u>	<u>(251,586)</u>
Administrative Expenses			
VLCT services	108,404	107,323	1,081
Claims services	34,500	34,388	112
Data services	22,000	25,864	(3,864)
Consulting	-	30,794	(30,794)
Legal services	5,000	4,879	121
Audit and accounting services	8,500	8,527	(27)
Actuarial services	8,000	5,197	2,803
Bank costs	2,400	3,298	(898)
Investment consulting fees	1,500	1,346	154
Investment management fees	2,400	2,957	(557)
Insurance	2,000	1,114	886
Board of Directors	7,000	7,292	(292)
Board travel and training	3,000	1,580	1,420
Staff travel and training	4,100	4,546	(446)
Vehicle expenses	953	113	840
Program supplies	100	-	100
Dues and subscriptions	1,400	1,230	170
Town Fair	1,000	-	1,000
Miscellaneous	-	189	(189)
Total administrative expenses	<u>212,257</u>	<u>240,637</u>	<u>(28,380)</u>
Member Relations			
VLCT services	11,441	11,437	4
Staff travel and training	200	23	177
Vehicle expense	477	669	(192)
Program supplies	-	88	(88)
Promotionals	100	290	(190)
Miscellaneous	-	3,810	(3,810)
Total member relations expenses	<u>12,218</u>	<u>16,317</u>	<u>(4,099)</u>
Claims benefits payments	<u>900,323</u>	<u>433,869</u>	<u>466,454</u>
Total expenses	<u>1,124,798</u>	<u>690,823</u>	<u>433,975</u>
Excess of Revenues over Expenses	<u>\$ (8,789)</u>	<u>\$ 173,600</u>	<u>\$ 182,389</u>