PUBLIC AGENCY COMPENSATION TRUST

FINANCIAL STATEMENTS

June 30, 2012 and 2011

CONTENTS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Public Agency Compensation Trust

We have audited the accompanying statement of net assets of the Public Agency Compensation Trust as of June 30, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets, and the statements of cash flows for the years then ended. These financial statements are the responsibility of the organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above presents fairly, in all material respects, the financial position of the Public Agency Compensation Trust as of June 30, 2012 and 2011 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the supplemental section, which includes the 10 Year Claims Development schedule, are not a required part of the basic financial statement, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedure, which consisted principally of inquires of management regarding the methods of measurements and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The supplemental schedule on unpaid loss liabilities for the Worker's compensation and Heart & Lung funds, Comparative Schedule of Claim Development for Workers Comp and Heart & Lung, the statutory Schedule P requirements and investment schedules prepared in NAIC format is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we express no opinion those schedules.

Bertrand & Associates, LLC

October 18, 2012
Carson City, Nevada

Management's Discussion and Analysis

Purpose:

To further understanding of significant financial issues, this Public Agency Compensation Trust management's discussion and analysis a) provides an overview of PACT's financial activities, b) identifies significant changes in PACT's financial position and its ability to address subsequent year financial challenges and c) provides insights into the long-term financial viability of PACT.

Background:

As a result of changes in the Governmental Accounting Standards Board (GASB) requirements set forth in GASB Statement No. 34 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Government,* PACT's financial information must be accompanied by enhanced analysis, both short and long term, and explanations of significant financial statement elements. Since Public Agency Compensation Trust operates as an enterprise created pursuant to NRS 277, the Interlocal Cooperation Act, its financial statements will be presented in a manner that reflects its operations much like a private company. PACT also is regulated by the Nevada Division of Insurance as an association of self-insured public agencies and must file certain financial schedules in addition to the GASB required information.

Using this Annual Report:

Since the financial statements report information about PACT using accounting methods similar to those used by private sector organizations, these statements offer short and long term financial information about PACT's activity. The financial statements show a comparison of two audited years ending June 30, 2012 and June 30, 2011 to facilitate understanding of changes in the financial position over time.

The Statement of Net Assets includes all of PACT's assets and liabilities and information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for computing rate of return, evaluation of the capital structure and for assessing the liquidity and financial flexibility of PACT.

Current year revenues and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Assets. This statement measures the success of PACT's operations for the fiscal year compared to the previous year and can be used as a measure of PACT's credit worthiness and whether PACT successfully recovers its costs through its sources of revenue.

The Statement of Cash Flows serves to provide information about PACT's cash receipts and cash payments during the reporting period. The statement reports cash receipts, cash payments and net changes in cash resulting from operations and investments. It also discloses from where cash comes, for what it was used and the change in cash balance during the reporting period. Since PACT incurs financial obligations to pay for claims that occurred in the past from current year resources and at the same time receives revenue that it must retain for payment of future claims from future resources, cash flow may vary significantly from year to year.

Financial Highlights:

Statutory requirements and board policy require PACT to be audited each year by an independent auditor. Since its inception on April 1, 1996 and continuing through this fiscal year, the independent auditor's report offers an unqualified opinion on the financial statements. Such an opinion reflects the highest opinion that can be obtained from an independent auditor.

<u>Changes in net assets:</u>
Fiscal year ended June 30, 2012: $46,546,686
Fiscal year ended June 30, 2011: $48,159,833
Net decrease: ($1,613,147) or (3.9) %.

PACT's primary revenue source comes from Member contributions to PACT's Loss Fund, administrative budget and reinsurance and excess insurance costs. Interest income on investments constitutes the secondary revenue source.

<u>Total assessments revenues:</u>
Fiscal year ended June 30, 2012: $13,740,006
Fiscal year ended June 30, 2011: $12,778,111
Net increase: $961,895 or 7.5%.

The increase resulted from increased rates.
<u>Total expenses:</u>
Fiscal year ended June 30, 2012: $17,843,024
Fiscal year ended June 30, 2011: $13,916,733
Net increase: $3,926,291 or 28.2%.

The most significant factors in this change are attributable to increased amortization expense and the significant increase in claims reserves. The amortization expense is attributable to PACT's further contribution of surplus to Public Compensation Mutual (PCM), its captive insurance company. The development schedule included in the financial statement provides the history of the claims reserve changes each year over 10 years.

<u>Operating net assets:</u>
Fiscal year ended June 30, 2012: $(4,103,018)
Fiscal year ended June 30, 2011: $(1,138,622)
Net decrease: $(2,964,396)

The most significant contributor to the decrease in operating net assets came from claims reserves which increased $2,989,246, thus contributing 73% of the decrease. Increases in amortization expenses contributed $430,918 or 11% of the decrease in operating net assets. Increased amortization expense reflects the board's decision to increase contributions to surplus to PCM consistent with its long-term strategy. The Insurance Division Fees contributed $781,115 or 19% of the increased expenses due to higher regulatory budgets and a substantial increase in the subsequent injury fund assessment.

<u>Net investment income:</u>
Fiscal year ended June 30, 2012: $2,489,871
Fiscal year ended June 30, 2011: $1,409,777
Net increase: $1,080,094

Investments are marked to market value at the time of the financial statements, which may result in a negative or positive overall result. Maintaining positive returns under the difficult economic conditions during this fiscal year speaks to the conservative investment strategies employed by PACT. The investment portfolio consists of governmental type investments which, if held to maturity, will yield the respective coupon rates although interim performance may lag. Most of PACT's investments are anticipated to be held to maturity.

Financial Analysis:

In order to enhance analysis, comparative information is provided for assets, liabilities, net equity, revenues and expenses as shown in the chart at the end of this narrative. The benchmarks shown in the chart resulted from a pooling and captives' industry study conducted a few years ago by Tillinghast and provides a useful tool to facilitate management's analysis and understanding of the financial results. Other performance indicators may be used by insurance companies but are not necessarily useful comparative indicators for risk pools.

Assets:

In fiscal year ended June 30, 2012, net assets declined by (3.3) % or $1,613,147. This result substantially is less than the modest gain of the previous fiscal year largely due to the increased claims reserves, amortization of PCM contributions and the regulatory fee increase. . An explanation about how these results were achieved was provided in the financial highlights. Continuing to grow the asset base is critical to the long term viability and stability of PACT due to the volatility of workers compensation claims and the level of retention taken by PACT. A strong base enables PACT to withstand a substantial reversal in incurred claims costs due to catastrophes or substantially increased high cost claims frequency. PACT's Board policies require a strong, sustainable and durable financial condition to avoid adversity. Workers compensation is a volatile business, thus attention to long term strategies to maintain net assets is critical to success.

Revenues, Expenses and Changes in Assets:

Gross revenues (assessments plus net investment income) increased by 7.5% for fiscal year ended June 30, 2012 as a result of a rate increase and improvements in the net investment income.

Actuarial

The actuarial analysis for the current fiscal year revealed a substantial increase in case reserves and IBNR reserves over prior years' estimated incurred losses. Refer to Note 13 for the details of Unpaid Loss Liabilities.

Other factors also apply: 1) Alternative Risk Services' (ASC -PACT's claims administrator) experienced adjusters have been able to manage claims efficiently and effectively and have maintained quality as evidenced by external claims audits; however, adverse development of claims reserves on a few claims contributed to the increased actuarial reserves 2) SpecialtyHealth, the managed care organization and bill reviewer for PACT has greatly helped the adjusters manage claims effectively, 3) loss control efforts have proven effective and further initiatives are being implemented, and 4) the continuing roll-out of the Cardiac Wellness Program that should help reduce potential heart claims, although implementation impediments continue to slow down the program. It is important to continue to strengthen these approaches to assure continued success for PACT.

Workers compensation self-funded programs experience significant volatility particularly when the retention levels per loss are high. Because PACT retains a substantial portion of the risk in all classifications, it is important to the long term viability of PACT and to assure its ability to meet its obligations to injured workers that PACT grow its net assets. We continue to face pressure to increase our retentions in light of medical and wage inflation trends as well as market pressures, which suggests that volatility will further increase and will need to be cushioned strongly. By growing net assets strongly, PACT is better positioned to respond to these demands while maintaining financial stability. PACT management, consistent with board policy, selected a 75% actuarial confidence level as a prudent level to develop a strong financial position in keeping with the PACT Board's goals of creating and sustaining a durable financial position.

Capital Assets and Debt Administration:

PACT has no physical assets and no debt. It has pledged certain investments to satisfy a regulatory solvency security requirement and thus, cannot access those funds without approval from the Nevada Division of Insurance.

Economic Factors:

For fiscal year ending June 30, 2012, economic conditions showed signs of continued uncertainty with tepid growth beginning to appear for the nation and Nevada. Medical inflation moderated nationally but still exceeds the general inflation rate and this affects the underlying costs of claims payable by PACT. While Nevada retains a fee schedule to limit cost increases, recent reviews of the fee schedule components resulted in increases in the last few years. Wage inflation generally is low in the public sector, which keeps disability costs down. A legislative change in 2003 resulted in adoption of the 5th Edition of the AMA guide to rating impairments, which increased costs overall. The 2009 Legislature fixed the 5th Edition into statute rather than having the most current edition be implemented by regulation. The 6th edition would have reduced costs in several key ratings of impairments due to recognition of improved medical outcomes.

The Nevada Supreme Court reached a decision in 1998 interpreting the special provisions for heart and lung coverage for qualifying police officers and firefighters that concluded that once these persons meet the five years of continuous service eligibility for benefits, those benefits are available for life regardless of any connection to actual work at the time the claims is made. Staff immediately implemented a judgment loading in the rates for this new interpretation of the statute, pending legislative action. PACT unsuccessfully attempted to have the Legislature modify this court interpretation to require that the claim must manifest within a reasonable time frame from leaving the workplace. As a result of that failed effort, PACT undertook an actuarial study to estimate the lifetime cost of risk associated with this decision. That study was concluded and the results indicated that the present value of the future benefits for former employees was estimated to range from $5,668,000 to $22,258,000, depending upon the interpretation as to which legal theory may be applicable. A subsequent actuarial study confirmed a change in the range of values to between twenty and eight million, again depending upon the assumptions made about claims manifestation.

These figures were presented to a task force who recommended to the board that they eliminate the judgment loading and implement a funding plan based on the actuarial study effective with the subsequent fiscal year. The board adopted the funding plan for implementation effective July 1, 2002. By taking this action, the board began its mitigation plan for the long-term adverse financial impact of the risk of former police officers and firefighters filing workers compensation claims long after employment. Subsequently, the board authorized acceleration of the funding rate. The rate set in 2002 was increased by 10% as a result of the second actuarial study that increased the range of potential losses from prior studies and demonstrated the need to accelerate needed assessments in future fiscal years as demographic factors begin to influence the post-employment risks.

The heart/lung assessments collected for fiscal year ended June 30, 2012 were $1,634,083 compared to June 30, 2011 were $1,503,026 even though PACT had one large member withdraw on July 1, 2010.

PACT sought relief before the United States Supreme Court to address the question of the constitutionality of the post employment conclusive presumption of eligibility for workers compensation for police officers and firefighters, but was denied review.

We continue to experience adverse rulings at hearing and appeal levels regarding heart-lung cases. Political actions to increase benefits continues each legislative session, particularly by law enforcement and firefighter lobbyists, and that causes pressure by excess insurers and reinsurers to increase PACT’s retention or cause increased costs or both, which would require rate increases or weaken the financial position. Demographically, there is an emerging and accelerating likelihood of additional heart-lung claims from both current and post-employment eligible law enforcement officers and firefighters. PACT supported a bill brought forth in 2011 by Sen. Rhoades on behalf of the Nevada Taxpayers Association that would have capped post-employment eligibility, but the bill died in the Assembly.

Subsequent Events:

There were no subsequent events that would affect the financial statements for the current fiscal year.

Requests for Information:

While the purpose of this discussion and financial report is to provide a general overview of PACT’s financial position, requests for additional financial information should be addressed to Wayne Carlson, Executive Director, 201 S. Roop St., Suite 102, Carson City, NV 89701-4790.

Wayne Carlson
Executive Director, Public Agency Compensation Trust

Financial Ratios	2007/2008	2008/2009	2009/2010	2010/2011	2011/2012
Total Revenue	$ 15,746,515	$ 14,978,027	$ 14,043,571	$ 12,778,111	$ 13,740,006
Revenue over (under) Expenses	$ 8,964,327	$ 4,473,424	$ 2,217,070	$ 271,155	$ (1,613,147)
Net Operating Income	$ 5,493,640	$ 1,069,234	$ (595,858)	$ (1,138,622)	$ (4,103,018)
Net Investment Income	$ 3,467,687	$ 3,404,190	$ 2,812,928	$ 1,409,777	$ 2,489,871
Total Assets	$ 60,092,890	$ 67,664,744	$ 73,829,771	$ 76,488,418	$ 79,370,901
Total Liabilities	$ 18,894,706	$ 21,993,136	$ 25,941,093	$ 28,328,585	$ 32,824,215
Net Assets	$ 41,198,184	$ 45,671,608	$ 47,888,678	$ 48,159,833	$ 46,546,686
Net Assets to SIR (Board Target 12:1); Benchmark >5:1	80.78	89.55	93.90	94.43	93.09
SIR to Net Assets (Benchmark: captives <.10; group capitves <.25)	0.01	0.01	0.01	0.01	0.01
% Assets attributable to Net Assets	68.6%	67.5%	64.9%	63.0%	58.6%
Total assets/total liabilities	3.18	3.08	2.85	2.70	2.42
Revenues to Net Assets (Benchmark: <2.5:1 and >0	0.38	0.33	0.29	0.27	0.30
Loss Reserves to Net Assets (discounted): Benchmark <3:1 and >0	0.31	0.33	0.35	0.37	0.41
Total liabilities to liquid assets: Benchmark <100%	40%	43%	47%	51%	54%
Change in members' Net Assets: >-10%	27.8%	10.9%	4.9%	0.6%	-3.3%
Return on Net Assets: Net Operating Income/Net Assets	13.3%	2.3%	-1.2%	-2.4%	-8.8%
Return on Net Assets: Total Income/Net Assets	21.8%	9.8%	4.6%	0.6%	-3.5%

PUBLIC AGENCY COMPENSATION TRUST
STATEMENTS OF NET ASSETS
June 30, 2012 and 2011

ASSETS	**2012**	**2011**
Current assets:		
Cash and cash equivalents - Note 2	$ 917,127	$ 3,207,550
Investments - Note 3	51,135,355	44,969,712
Investment income receivable - Note 3	372,481	347,173
Member assessments receivable Note 4	3,427,253	3,369,665
Specific recoverable	84,625	68,570
Prepaid expenses	68,062	81,366
Total current assets	56,004,903	52,044,036
Other assets:		
Pledged investments - Note 3	4,229,358	4,183,609
Contributed surplus PCM, net - Note 14	19,136,640	20,260,673
Total Assets	**$ 79,370,901**	**$ 76,488,318**
LIABILITIES		
Current liabilities:		
Accounts payable	$ 82,382	$ 44,889
Specific recoverable	84,625	68,571
Current portion of reserve for losses and expenses - Note 13	6,474,150	5,798,385
Total current liabilities	6,641,157	5,911,845
Noncurrent liabilities:		
Reserve for losses and loss adjustment expenses, net current portion - Note 13	14,696,850	12,564,615
Heart and Lung expense reserve - Note 9	11,486,208	9,852,125
Total non-current liabilities	26,183,058	22,416,740
NET ASSETS		
Net assets-unrestricted	46,546,686	48,159,833
Total Liabilities & Net Assets	**$ 79,370,901**	**$ 76,488,418**

See accompanying notes

PUBLIC AGENCY COMPENSATION TRUST
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
Years ended June 30, 2012 and 2011

	2012	2011
REVENUES:		
Assessments for workers compensation	$ 12,104,713	$ 11,275,085
Assessments for heart and lung	1,634,083	1,503,026
Agent commissions	1,210	-
Total Revenues	13,740,006	12,778,111
LOSS FUND AND PROGRAM EXPENSES:		
Claims and adjustment expenses	9,301,255	6,312,209
Heart and Lung loss expenses	1,634,083	1,503,026
Excess insurance premium	577,229	537,039
Re-insurance premium	244,000	223,667
Underwriting and claims processing	699,641	642,021
Total loss fund and program expenses	12,456,208	9,217,962
ADMINISTRATION EXPENSES:		
Management fees	462,000	471,955
Professional services	90,544	77,240
Administrative and overhead	251,587	239,216
Member education and services	711,057	677,099
Insurance Division fees	781,115	572,784
Insolvency fund and related expenses	14,819	15,800
Loss control expenses	409,599	409,500
Amortization expense	2,666,095	2,235,177
Total administration expenses	5,386,816	4,698,771
Increase (decrease) in operating net assets	**(4,103,018)**	**(1,138,622)**
Increase in non-operating net investment income	2,489,871	1,409,777
Increase in net assets	**(1,613,147)**	**271,155**
Net assets, beginning of year	48,159,833	47,888,678
Net assets, end of year	**$ 46,546,686**	**$ 48,159,833**

See accompanying notes

PUBLIC AGENCY COMPENSATION TRUST
STATEMENTS OF CASH FLOWS
For Years Ended June 30, 2012 and 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Assessments and other revenues	$ 13,681,207	$ 12,960,783
Payment for claims	(6,493,255)	(5,172,234)
Payment to vendors	(4,189,584)	(4,182,074)
Net cash provided from operating activities	2,998,368	3,606,475
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Contributed surplus of Public Compensation Mutual	(1,542,062)	(7,517,375)
Net cash used for capital and related financing activities	(1,542,062)	(7,517,375)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest and net realized investment income	1,551,830	2,151,013
Sale of investments	-	2,896,750
Purchases of investments	(5,298,559)	(2,374,578)
Net cash provided (used) for investing activities	(3,746,729)	2,673,185
Decrease in cash and cash equivalents	(2,290,423)	(1,237,715)
Cash and cash equivalents, beginning of fiscal year	3,207,550	4,445,265
Cash and cash cquivalents, year ended June 30	**$ 917,127**	**$ 3,207,550**
RECONCILIATION FOR OPERATING INCOME TO NET CASH PROVIDED BY OPERATNG ACTIVITIES		
Operating net loss	$ (4,103,018)	$ (1,138,622)
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Member assessments receivable	(57,589)	182,672
Specific recoverable	(16,054)	(3,153)
Prepaid expenses	13,306	(57,092)
Accounts payable	37,491	(258,660)
Specific recoverable	16,054	3,153
Amortization of contributed surplus	2,666,095	2,235,177
Loss reserves	4,442,083	2,643,000
Net cash provided by operating activities	**$ 2,998,368**	**$ 3,606,475**

See accompanying notes

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of program

Public Agency Compensation Trust (PACT) was formed by local governments for the purpose of organizing a self-insured workers' compensation group. The Trust began operations April 1, 1996. The trust's objective is to provide members with a lower cost alternative achieved through enhanced claims management, program administration, and member services that will reduce the cost of claims.

PACT provides workers' compensation coverage to member governmental entities and hospitals pursuant to state statutes. The program is fully funded by member entities and is governed by a Board of Trustees comprised of representatives of each member. Any member may withdraw from the program by giving 120 days notice. PACT's independent actuary, who is an approved Rate Service Organization, develops PACT rates.

Principles of presentation

PACT has prepared its financial statements in accordance with accounting principles generally accepted in the United States of America. PACT prepares its financial statements on the accrual method of accounting recognizing income when earned and expenses when incurred. PACT has implemented Governmental Accounting Standards Board (GASB) Statements No. 34 and No. 37, *Basic Financial Statements - and Management's Discussion and Analysis – for State and Local Governments and GASB Statement 38, Certain Financial Statement Note Disclosures.*

The financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America for governmental entities and insurance enterprises, where applicable, which may differ from the basis of accounting followed in statutory reporting.

Accounting principles generally accepted in the United States of America require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Measurement focus and basis of accounting

The financial statements are reported using the economic resources management focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows. Expenditures are recorded when the related fund liability is incurred.

Cash and cash equivalents

The Operating Fund has a checking account, money market investment account, and an investment account for long-term investments. For the purposes of the Statement of Cash Flows, the PACT considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents. The Claims Fund has two checking accounts, one for payment of claims and the other for claims related expenses as required by Nevada Revised Statute 616B.368.

Investments and investment income

Investments consist predominately of government and government backed securities and are reported at their fair value in the statement of position. Fair value is determined utilizing the market value of the investments as reflected on the applicable brokerage statements. Net increases and decreases in the fair value are included in the statement of activities and changes in fund balances.

PACT is authorized to make investments in bonds and debentures of the United States, bills and notes of the U.S. Treasury, and in high-grade equity securities. PACT also is authorized to purchase negotiable certificates of deposit issued by commercial banks or insured savings and loan associations. PACT's investments have been restricted by policy of the Board to those allowable for local governments.

Budget

A budget is prepared by management but there is no legal budgetary requirement.

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Credit Risk:
Credit risk is the risk that the issuer of a security will default on principal and interest of the security. PACT's policy is to invest in corporate debt issues with a minimum of an "AA" rating from Moody's or Standard and Poor's rating services or U.S. Government and government backed securities. In addition, PACT's policy is to diversify the investment portfolio so that the impact of potential losses from any one type of security or from any one issuer will be minimized.

Concentration of Credit Risk: PACT limits investments in fixed income securities to 10% of the total fixed income portfolio to any one issuer. No more than 15% of the total investment pool will be invested in any one class of security, industry or company. PACT will not directly invest in securities maturing more than ten (10) years from the date of purchase, except as permitted by law. The policy does not place a limit on the purchase of U.S. Government and government backed securities.

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. PACT will, to the extent possible, minimize this risk by matching investment maturities to liability due dates. This allows PACT to hold investments to maturity thus mitigating losses from the sale of investments prior to their maturity date. Additionally, exposure to fair value losses arising from decreasing interest rates is minimized by investing predominantly in investments with short to mid-term maturities that perform in line with the return of a managed fund comprised of 1 – 3 year Treasury Bonds.

Member Assessments
Member assessments and reports are due 20 days after the end of the quarter. Assessment rates are based on independent actuarial estimates that are reviewed and approved by the Insurance Commissioner.

Losses and loss adjustment expense
Reserves for losses and allocated loss adjustment expenses are provided based on case-based estimates for losses reported and PACT's historical loss experience for claims incurred but not reported (IBNR). The liability for unpaid losses and loss adjustment expenses includes the estimated cost of investigating and settling all claims incurred as of the balance sheet date. Such amounts are determined based on an evaluation prepared by management and an independent consulting actuary. Although such estimates are best estimates of the expected values, the actual results may vary from these values.

The liability represents the estimated ultimate cost of settling claims, including the effects of inflation and other societal and economic factors. The liability also includes unallocated costs which are estimated by management. Any adjustments resulting from the settlement of losses will be reflected in earnings at the time the adjustments are determined. The loss reserve estimates are discounted at 3% in 2012 and 2011, the expected investment rate, to show the present value of those reserves.

Income Taxes
In accordance with Internal Revenue Service code Section 115, organizations formed, operated and funded by political subdivisions may exclude income from those activities that qualify for exclusion. Accordingly, no provision for income taxes has been provided in the accompanying financial statements.

Insurance Division Annual Fees
The Insurance Division annually assesses fees to the Trust based on prior year's claims expenditures. It is the policy of management to record the invoice received each year as the expense for that year as these invoices cannot be reasonably estimated and therefore accrued.

Supplementary development schedule - Unaudited
The statements and development schedule reports claims paid on a reported year basis. Loss reserves shown on the financial statements are discounted; however, the development schedule reflects undiscounted loss reserves.

Prior year's reclassification
The prior year's financial statements have been reclassified were applicable to conform to current year's presentation.

NOTE 2 – CASH & EQUIVALENTS

The carrying amount of PACT's deposits with financial institutions at June 30, 2012 and 2011 are $917,127 and $3,207,550 respectively. The financial institution balances were $1,040,152 and $3,384,389 respectively. The difference between the carrying amounts and financial institution balances results from outstanding checks and deposits not yet reflected in the bank's records.

	2012	2011
Amounts insured by FDIC	$250,000	$250,000
Amounts collateralized	307,363	1,176,896
Cash equivalents at brokerage firm	482,789	1,957,493
Total deposits at financial institutions	$1,040,152	$3,384,389

PACT maintains its cash, cash equivalents and investments in a commercial bank and a brokerage institution. All amounts in the commercial bank are insured by the FDIC or collateralized. Amounts at the brokerage firm up to the SPIC insurance limit are insured through SPIC and additional amounts are insured by the broker through an insurance policy.

NOTE 3 – INVESTMENT SECURITIES

A summary of investments as of June 30, 2012 is as follows:

		Investment Maturities in Years			
	Fair Value	**1 year of less**	**1-5**	**5-10**	**Over 10**
U.S. Treasuries	$ 17,554,956	$ -	$ 10,057,974	$ 7,496,982	$ -
U.S. Government & Agencies	$ 16,582,502	502,447	8,112,421	2,371,239	5,596,395
U.S. Mortgage-backed securities	$ 11,781,540	2,604,257	4,846,845	3,103,090	1,227,348
U.S. Government backed securities	$ 9,445,715	126,786	-	547,436	8,771,493
Less pledged investements	$ (4,229,358)	-	(3,519,390)	(709,968)	-
Total cash and investments	$ 51,135,355	$ 3,233,490	$ 19,497,850	$ 12,808,779	$ 15,595,236

A summary of investments as of June 30, 2011 is as follows:

		Investment Maturities in Years			
	Fair Value	**1 year of less**	**1-5**	**5-10**	**Over 10**
U.S. Treasuries	$ 15,796,766	1,126,221	1,791,020	12,879,525	-
U.S. Government & Agencies	$ 8,911,858	695,358	5,644,666	2,284,891	286,943
U.S. Mortgage-backed securities	$ 2,736,246	-	443,661	61,038	2,231,547
U.S. Government backed securities	$ 21,708,451	8,332,785	9,732,939	3,056,486	586,241
Less pledged investements	$ (4,183,609)	-	-	(4,183,609)	-
Total cash and investments	$ 44,969,712	$ 10,154,364	$ 17,612,286	$ 14,098,331	$ 3,104,731

Investment income receivable was $372,481 on June 30, 2012 and $347,173 on June 30, 2011.

Actual maturities may differ from contractual maturities as some borrows have the right to call or prepay with or without call or prepayment penalties. Restricted investments are those investments pledged to Insurance Commission. Investments are reported at fair value by the investment broker as determined by an outside pricing firm. All securities are U.S Government or government backed.

NOTE 4 – MEMBER ASSESSMENTS RECEIVABLE
Member assessments receivable were $3,427,253 and $3,369,665 for the years ended June 30, 2012 and 2011. Amounts receivable at both years' end are primarily assessments for the last quarter of the fiscal year and are determined based on the annual payroll audits.

NOTE 5 – LIABILITY OF MEMBERSHIP
Members of PACT are jointly and severally liable to pay benefits to injured workers as required by law. Workers compensation pools can be subject to assessments by the Insurance Commissioner should other self-insured workers compensation pools encounter financial difficulties.

NOTE 6 – REINSURANCE & EXCESS INSURANCE
In the ordinary course of business, PACT maintains both reinsurance and excess insurance contracts with various insurance carriers through their broker company, Willis Pooling. These reinsurance and excess insurance contracts provide both a specific and an aggregate limit of liability to protect PACT against potentially large losses or an accumulation of losses. This provides coverage in excess of PACT's self-insured retention. The limits provided by these reinsurance and excess insurance contracts, including PACT's self-insurance retention, are as follows:

1) The specific limit of liability per accident is statutory excess of a self-insured retention per accident of $2,500,000. PACT reinsures a portion of PACT's limit of indemnity of $2,500,000 through Public Compensation Mutual, which bears 25% of $2,000,000 excess of PACT's $500,000 retention and through County Reinsurance, LTD., which bears 75% of $2,000,000 excess of PACT's $500,000 retention

2) A limit of liability of $3,000,000 excess of an aggregate retention of $2.83 per $100 of payroll, subject to a minimum aggregate retention of $8,394,594 and $8,397,190 for years ended June 30, 2012 and 2011. PACT reinsures a portion of PACT's aggregate excess limit of $3,000,000 through Public Compensation Mutual which bears $1,500,000 of PACT's annual aggregate excess limit and through $Safety National Casualty Company which bears $1,500,000 of PACT's annual aggregate excess limit.

Both Public Compensation Mutual and County Reinsurance, Ltd. are captive insurance companies in which PACT has a financial interest.

NOTE 7 - RELATED PARTY TRANSACTIONS
Public Agency Risk Management Services, Inc. (PARMS) is presently contracted to provide management services. PARMS serves both PACT and the Nevada Public Agency Insurance Pool (POOL) as the Executive Director/Administrator. PARMS is a service corporation wholly owned by Mr. Wayne Carlson. Management fee paid under the contract for years ended June 30, 2012 and 2011 was $462,000 and $471,955 respectively. The management contract agreement was renewed with PARMS commencing July 1, 2012 and terminating on July 1, 2014 with an option to extend with the same terms and conditions for an additional two years. A 3% annual increase for management fees is included in the contract.

PARMS is under obligation to lease office space from the Nevada Public Agency Insurance Pool throughout the term of the management contract. Payments made in 2012 and 2011 were $63,864 and $62,004. The contract includes a 3% per annum increase in the lease expenses.

Many of the board members of the Nevada Public Agency Insurance Pool (POOL) are also members of PACT as they share a common membership. The board of Public Compensation Mutual comprises of several PACT board members. Nevada Association of Counties (NACO) is a member of PACT and was a tenant until January 1, 2012.

NOTE 7 - RELATED PARTY TRANSACTIONS (continued)

Effective July 1, 2006, NPAIP jointly with PACT provided a grant with Pooling Resources, Inc. (PRI), a nonprofit organization formed by the executive director of NPAIP, Wayne Carlson, and whose directors are Wayne Carlson, Alan Kalt and Michael Rebaleati. The cost of this grant was $583,500 and $566,000 for 2012 and 2011 respectively. The grant was renewed for three years beginning July 1, 2012 with future costs being $525,000, $535,500 and $546,500 for years ended June 30, 2013, 2014 and 2015 respectively. PRI provides human resources management services to PACT members. PRI pays PARMS a management fee to provide operational and financial oversight of PRI.

NOTE 8 – PLEDGED INVESTMENTS & UNUSED LETTER OF CREDIT

According to NRS 616B.353.1(d) and (e) and related regulations, an association of self-insured employers must deposit with the Commissioner a bond or other authorized security, payable to reasonably secure payment of the workers compensation benefits to employees

PACT has obtained a letter of credit from Wells Fargo Bank with the named beneficiary being the State of Nevada Division of Insurance. In April of 2011, PACT decided to not renew the letter of credit and instead pledged certain investments to secure payment. The amounts pledged at June 30, 2012 were $4,229,358 and $4,183,609. In the event that PACT becomes delinquent in its payment of workers compensation benefits, the proceeds will be used to satisfy losses, costs or expenses incurred by the Insurance Division.

NOTE 9 – HEART AND LUNG LOSS FUND

The Heart and Lung Loss Fund reflects special reserves set aside for the purpose of covering post-employment heart or lung disease claims that may be the responsibility of PACT members pursuant to the Last Injurious Exposure Rule interpretation of the law and court cases that determined that coverage for such claims applies to former employees who meet the statutory eligibility requirements for the heart and lung disease benefit

Post-employment claims historically have not been reflected in rate classifications for the appropriate police officer and firefighter classifications. The actuarial projections of loss and loss adjustment expense are intended to be fully funded, thus assessments for this fund are offset 100% by claims reserves. Management followed this conservative approach because of the uncertainty and volatility inherent in this specific risk. The reserve for 2012 and 2011 is $11,486,208 and $9,852,125 respectively.

NOTE 10 – ALLOCATION OF ASSESSMENTS REVENUES

The Nevada Revised Statute 616B.368 requires that 75% of assessment revenues collected be placed in a separate account and that disbursements from this account be limited to paying claims, claims related expenses, excess insurance costs, assessments, payments and penalties related to the subsequent injury fund and the uninsured employer's claim fund. Initially, all funds collected for member assessments and prepayments of assessments and deposits are deposited into the operating account. Periodically, 75% of the assessments are transferred to a separate bank or investment account to comply with this statute.

NOTE 11 – POOLING RESOURCES INC.

Pooling Resources Inc. is required to provide status reports and quarterly financial statements to the POOL and PACT Executive Committees according to the grant document. A renewal of this contract was made for three years beginning July 1, 2012. PACT’s share of the cost is for the first year is $525,000, $535,500 for the second year and $546,500 for the third year.

NOTE 12 –SUBSEQUENT EVENTS

Management has evaluated the activities and transactions subsequent to June 30, 2012 to determine the need for any adjustments to, and disclosure within the financial statements for the year ended June 30, 2012. Management has evaluated subsequent events through October 18, 2012 which is the date the financial statements were available for issue.

NOTE 13 – UNPAID LOSS LIABILITIES

PACT establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related loss adjustment expenses. The following represents changes in those aggregate liabilities during the years ended June 30, 2012 and 2011:

	2012	2011
Unpaid losses and loss adjustment expenses at beginning of year or period	**$ 28,215,125**	**$ 25,572,125**
Incurred losses and loss adjustment expenses:		
Provision for insured events of current year	8,749,083	7,643,209
Increase in provision for insured events of prior fiscal years	2,186,255	172,000
Total incurred losses and loss adjustment	10,935,338	7,815,209
Payments:		
Claims and claim adjustment expenses attributable to insured events of current fiscal year/period	(1,875,000)	(1,627,000)
Claims and claims adjustment expenses attributable to insured events of prior	(4,618,255)	(3,545,209)
Total Payments	(6,493,255)	(5,172,209)
Unpaid claims and claims adjustment expenses At end of fiscal year	**$ 32,657,208**	**$ 28,215,125**

The current portion of the long term loss reserve for 2012 and 2011 is $6,474,150 and $5,798,385 with the long term portion for 2012 and 2011 being $26,183,058 and $22,416,740.

Incurred losses and loss adjustment expenses are comprised of two significant factors. Provisions for events of the current year increased from $7,643,209 for 2011 to $8,749,083 for 2012. The increase and decrease in the provision for insured events of prior fiscal years for 2012 and 2011 reflects changes in case reserves and actuarial reserve calculations for all prior years cumulatively.

Individual case reserves may increase or decrease as the case develops over time for various reasons. This may affect actuarial projections for past and future years since the various actuarial methodologies are based both on individual case reserve changes and long term trends in reserves. The effect of both the individual case reserve changes over time and the actuarial projections combined may result in a significant increase or decrease that is reflected in the current year's audited net assets. In other words, a decrease in reserves results in an increase in net assets, while an increase in reserves reduces net assets.

NOTE 14 – SURPLUS CONTRIBUTION TO PUBLIC COMPENSATION MUTUAL COMPANY

In May of 2007, PACT's board of directors authorized the start up of a member-owned nonprofit captive mutual insurance company and contributed surplus to the company in the amount of $5,000,000 and subsequent additional surplus contributions have been added. Capitalization at June 30, 2012 was $27,159,437 with accumulated amortization of $8,022,797 for a net amount of $ 19,136,640. Capitalization at June 30, 2011 was $25,617,375 with accumulated amortization of $5,356,702 for a net amount of $20,260,673.

The company, named Public Compensation Mutual, ("PCM") is domiciled in Nevada and as of July 1, 2007, became one of the workers compensation reinsurers for PACT. Some of the Public Compensation Mutual's board members also serve as board members of PACT.

Public Compensation Mutual was formed by members of PACT to reduce the costs of insurance, to obtain direct access to reinsurance, to provide broader coverage for policyholders, to broaden investment opportunities and to build equity to enable providing coverage not obtainable elsewhere.

As a condition of contributed surplus, but without any expectation that the funds will be returned, PACT required that prior to any distributions such as dividends, the contributed surplus must be repaid to PACT.

Management considers the contributed surplus costs a development cost that can provide lower operating costs in the future and estimates that the savings in reinsurance costs to PACT will recoup the start up capital. Therefore, the PACT's contributed surplus to PCM will be amortized over 10 years.

PUBLIC AGENCY COMPENSATION TRUST

Supplemental Schedule On Unpaid Loss Liabilities for Workers Compensation and Heart Lung

PACT establishes a liability for both reported and unreported insured events which includes estimates of both future payments of losses and related loss adjustment expenses. The following represents changes in those aggregate liabilities for the workers compensation and heart and lung coverages during the years ended June 30, 2012 and 2011:

	2012			2011		
	Workers Compensation	**Heart & Lung**	**Total**	**Workers Compensation**	**Heart & Lung**	**Total**
Unpaid losses and loss adjustment expenses at beginning of the year	$ 18,363,000	$ 9,852,125	$ 28,215,125	$ 17,223,000	$ 8,349,125	$ 25,572,125
Incurred losses and loss adjustment expenses:						
Provision for insured events of current year	7,115,000	1,634,083	8,749,083	6,140,209	1,503,000	7,643,209
Increase (decrease) in provision for insured events of prior fiscal year	2,186,255	-	2,186,255	172,000	-	172,000
Total incurred losses and loss adjustments	9,301,255	1,634,083	10,935,338	6,312,209	1,503,000	7,815,209
Payments:						
Claims and claim adjustment expense attributable to insured events of current year	(1,875,000)	-	(1,875,000)	(1,627,000)	-	(1,627,000)
Claims and claims adjustment expense Attributable to insured events of a prior period	(4,618,255)	-	(4,618,255)	(3,545,209)	-	(3,545,209)
Total payments	(6,493,255)	-	(6,493,255)	(5,172,209)	-	(5,172,209)
Unpaid claims and claims adjustments expenses at end of fiscal year	**$ 21,171,000**	**$ 11,486,208**	**$ 32,657,208**	**$ 18,363,000**	**$ 9,852,125**	**$ 28,215,125**

PUBLIC AGENCY COMPENSATION TRUST
COMPARATIVE SCHEDULE OF CLAIM DEVELOPMENT FOR WORKERS COMP AND HEART & LUNG – UNDISCOUNTED - (UNAUDITED)
EARNED ASSESSMENTS AND ALLOCATED EXPENSES FOR TEN-YEAR PERIOD - YEAR ENDED JUNE 30,

	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Required Contributions & Investment Income:										
Earned	$ 9,290,486	$ 11,609,553	$ 12,638,430	$14,150,771	$17,528,899	$19,214,202	$18,382,217	$16,856,499	$14,187,888	$16,229,877
Ceded	(481,095)	(551,944)	(789,791)	(626,266)	(673,485)	(711,236)	(999,595)	(1,019,746)	(760,706)	(821,229)
Net earned	8,809,391	11,057,609	11,848,639	13,524,505	16,855,414	18,502,966	17,382,622	15,836,753	13,427,182	15,408,648
Unallocated Expenses	2,378,840	2,753,420	2,280,908	2,401,410	2,644,815	3,467,687	3,888,708	4,372,365	5,340,792	6,086,457
Estimated Incurred Claims & Expense End of Policy Year:										
Incurred	5,721,353	7,611,959	7,694,786	7,221,184	6,932,261	6,211,000	6,699,000	7,604,904	7,226,000	8,393,000
Ceded	-	-	-	-	-	-	-	-	-	-
Net Incurred	5,721,353	7,611,959	7,694,786	7,221,184	6,932,261	6,211,000	6,699,000	7,604,904	7,226,000	8,393,000
Paid (cumulative) as of:										
End of policy year	1,059,764	815,018	1,153,042	903,024	955,534	1,396,400	1,813,443	1,576,283	1,627,122	1,875,562
One Year Later	2,242,826	1,833,437	2,466,279	1,863,166	2,333,923	3,334,645	3,630,752	3,121,442	3,604,503	
Two Years Later	2,581,248	2,286,157	2,774,180	2,317,418	3,332,247	4,312,797	4,050,129	4,039,612		
Three Years Later	2,780,197	2,624,047	3,033,660	2,626,506	3,930,487	4,768,994	4,496,682			
Four Years Later	2,898,113	2,864,122	3,323,358	2,872,958	4,102,622	5,095,774				
Five Years Later	2,892,851	2,995,578	3,399,607	3,226,213	4,388,188					
Six Years Later	2,979,779	3,209,246	3,454,799	3,457,294						
Seven Years Later	2,966,483	3,533,041	3,512,672							
Eight Years Later	2,997,581	3,749,627								
Nine Years Later	3,022,844									
Re-estimated ceded claims & Expenses	-	-	-	-	-	-	-	-	-	-
Re-estimated Claims & Expense										
End of policy year	5,721,353	7,611,959	7,964,786	7,221,184	6,932,261	6,211,000	6,699,000	7,604,904	7,226,026	8,403,083
One Year Later	5,823,353	6,558,041	5,783,000	5,100,000	6,163,261	7,066,000	7,100,000	7,767,000	8,156,000	
Two Years Later	5,006,353	4,952,041	5,147,000	4,117,000	7,269,261	7,695,000	6,892,000	8,507,000		
Three Years Later	4,285,353	4,645,041	5,230,000	4,388,000	7,555,261	7,612,000	7,010,000			
Four Years Later	4,114,353	4,941,041	5,287,000	4,574,184	7,453,261	8,127,000				
Five Years Later	4,093,535	4,870,041	5,238,899	4,729,000	7,650,261					
Six Years Later	3,617,000	5,260,041	5,235,000	4,819,000						
Seven Years Later	4,061,353	5,887,041	5,202,000							
Eight Years Later	4,059,353	5,814,041								
Nine Years Later	4,088,353									
Increase(Decrease) in Estimated Incurred Claims & Expenses from End of Policy Year:	**(1,662,000)**	**(1,724,918)**	**(2,729,786)**	**(2,492,184)**	**718,000**	**1,916,000**	**311,000**	**902,096**	**926,974**	-