

**LOCAL GOVERNMENT CENTER, INC.  
AND SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**

**and**

**SUPPLEMENTARY INFORMATION**

**December 31, 2009 and 2008**

**With Independent Auditors' Report**

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## INDEX

	<u>Page(s)</u>
Independent Auditors' Report	1-2
Consolidated Statements of Financial Position	3
Consolidated Statements of Revenues, Expenses, and Changes in Net Assets	4
Consolidated Statements of Cash Flows	5-6
Notes to Consolidated Financial Statements	7-23
Schedule of Funding Progress	24
Consolidating Schedule of Financial Position	25
Consolidating Schedule of Revenues, Expenses, and Changes in Net Assets	26
Consolidating Schedule of Cash Flows	27-28
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Accounting Standards</i>	29-30
Summary Schedule of Prior Audit Findings	31



## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Local Government Center, Inc. and Subsidiaries

We have audited the accompanying consolidated statements of financial position of Local Government Center, Inc. and Subsidiaries (LGC) as of December 31, 2009 and 2008 and the related consolidated statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of LGC's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Local Government Center, Inc. and Subsidiaries as of December 31, 2009 and 2008 and the consolidated changes in their net assets and their consolidated cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2010 on our consideration of LGC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying consolidated financial statements do not include required supplementary information, including management's discussion and analysis, reconciliation of claims liabilities by type of contract, and ten-year claims development information, which is supplementary information required by the Governmental Accounting Standards Board. The required supplementary information for the subsidiaries of LGC is included in their respective separately issued audited financial statements.

The historical pension information on page 24 is not a required part of the general purpose financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary information, included in pages 25 through 28, is presented for the purposes of additional analysis of the consolidated financial statements, rather than to present the financial position, changes in net assets or cash flows of the individual organizations. The supplementary information has been subjected to the audit procedures applied in the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

*Berry, Dunn, McNeil & Parker*

Manchester, New Hampshire  
June 18, 2010

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidated Statements of Financial Position**

**December 31, 2009 and 2008**

**ASSETS**

	<u>2009</u>	<u>2008</u>
Current assets		
Cash and cash equivalents	\$ 49,672,385	\$ 66,628,315
Investment securities	85,573,684	92,922,650
Investment in external investment pool	12,529,721	1,013,126
Contributions receivable	5,319,380	5,968,016
Accounts receivable	3,863,680	4,541,245
Claims recovery receivable	46,458	102,278
Accrued interest receivable	578,227	557,361
Prepaid expenses and deposits	<u>1,581,373</u>	<u>1,439,086</u>
Total current assets	<b>159,164,908</b>	173,172,077
Property and equipment, net	<b>11,410,696</b>	8,448,091
Restricted cash	<b>1,000,000</b>	1,000,000
Deposits	<u><b>1,407,738</b></u>	<u>1,407,738</u>
Total assets	<b><u>\$ 172,983,342</u></b>	<b><u>\$ 184,027,906</u></b>

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The accompanying notes are an integral part of these consolidated financial statements.

## LIABILITIES AND NET ASSETS

	<u>2009</u>	<u>2008</u>
Current liabilities		
Claims payable	\$ 11,372,830	\$ 9,702,827
Claims reserves	46,756,522	42,976,498
Claims adjustments and administrative reserves	3,284,409	1,677,000
Accounts payable and accrued expenses	3,649,010	7,102,416
Deposits and other current liabilities	883,110	1,076,750
Retainage payable	-	22,504
Unearned contributions	8,448,389	8,286,195
Defined benefit obligation	<u>23,652</u>	<u>-</u>
Total current liabilities and total liabilities	<u>74,417,922</u>	<u>70,844,190</u>
Commitments and contingencies (Notes 12, 13, 14, 16 and 18)		
Net assets (deficit)		
Unrestricted	(292,964)	32,305,999
Board designated	87,224,764	76,650,237
Restricted	254,513	168,430
Invested in capital assets	11,410,696	8,355,421
Unrealized loss on investment securities	<u>(31,589)</u>	<u>(4,296,371)</u>
Total net assets	<u>98,565,420</u>	<u>113,183,716</u>
Total liabilities and net assets	<u>\$ 172,983,342</u>	<u>\$ 184,027,906</u>

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**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidated Statements of Revenues, Expenses, and Changes in Net Assets**

**Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
Operating revenues		
Member contributions earned	\$ 389,030,884	\$ 363,260,831
Member contributions ceded	(5,538,079)	(5,006,450)
Self-funded plus program - net	(54,339)	322,493
Rent	13,490	11,415
Other revenue	<u>343,985</u>	<u>355,453</u>
Total net operating revenues	<u>383,795,941</u>	<u>358,943,742</u>
Operating expenses		
Claims incurred	369,314,907	321,381,823
Administrative fees	14,572,592	13,709,107
Other expenses	<u>22,621,081</u>	<u>21,432,931</u>
Total operating expenses	<u>406,508,580</u>	<u>356,523,861</u>
Operating (loss) income	(22,712,639)	2,419,881
Nonoperating income (expense)		
Investment income	3,724,764	4,187,974
Net increase (decrease) in fair value of investment securities	4,264,781	(5,502,856)
Other income	<u>104,798</u>	<u>89,854</u>
(Decrease) increase in net assets	(14,618,296)	1,194,853
Net assets, beginning of year	<u>113,183,716</u>	<u>111,988,863</u>
Net assets, end of year	<u>\$ 98,565,420</u>	<u>\$ 113,183,716</u>

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The accompanying notes are an integral part of these consolidated financial statements.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows**

**Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities		
Member contributions collected	\$ 389,898,450	\$ 362,359,991
Member contributions ceded to reinsurer	(6,028,890)	(4,834,349)
Restricted contributions received	107,722	184,441
Rental income collected	13,490	11,415
Other revenue received	206,761	154,181
Employee and other expenses paid	(34,982,399)	(28,801,566)
Claims paid	(363,841,094)	(318,453,315)
Loss prevention expenses paid	(2,892,478)	(1,911,242)
Net cash provided (used) by self-funded plus program	<u>270,618</u>	<u>(65,712)</u>
Net cash (used) provided by operating activities	<u>(17,247,820)</u>	<u>8,643,844</u>
Cash flows from investing activities		
Proceeds from the sale of investment securities	85,100,972	19,652,412
Interest and dividends on investment securities	3,768,952	4,035,098
Purchase of external investment pool	(9,494,039)	(2,048,135)
Purchase of investment securities	<u>(75,574,834)</u>	<u>(51,931,489)</u>
Net cash provided (used) by investing activities	<u>3,801,051</u>	<u>(30,292,114)</u>
Cash flows from capital and related financing activities		
Payment for construction of building and acquisition of capital assets	<u>(3,613,959)</u>	<u>(1,725,570)</u>
Net cash used by capital and related financing activities	<u>(3,613,959)</u>	<u>(1,725,570)</u>
Cash flows from noncapital financing activities		
Cash received from other income	<u>104,798</u>	<u>89,854</u>
Net cash provided by noncapital financing activities	<u>104,798</u>	<u>89,854</u>
Net decrease in cash and cash equivalents	(16,955,930)	(23,283,986)
Cash and cash equivalents at beginning of year	<u>66,628,315</u>	<u>89,912,301</u>
Cash and cash equivalents at end of year	\$ <u>49,672,385</u>	\$ <u>66,628,315</u>

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The accompanying notes are an integral part of these consolidated financial statements.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows (Concluded)**

**Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
Reconciliation of operating (loss) income to net cash (used) provided by operating activities		
Operating (loss) income	\$ (22,712,639)	\$ 2,419,881
Adjustments to reconcile operating (loss) income to net cash (used) provided by operating activities		
Depreciation and amortization	558,684	359,882
(Increase) decrease in		
Contributions receivable	659,811	(1,662,564)
Accounts receivable	666,390	(828,495)
Claims recovery receivable	55,820	170,008
Accrued interest receivable		(67,493)
Prepaid expenses and deposits	(142,287)	-
Increase (decrease) in		
Claims payable	1,670,003	130,885
Claims reserves	3,780,024	3,191,291
Claims adjustment reserves	1,607,409	339,000
Deposits held	(193,640)	(55,978)
Accounts payable and accrued expenses	(3,383,241)	3,882,589
Unearned contributions	162,194	764,838
Defined benefit obligation	<u>23,652</u>	<u>-</u>
Net cash (used) provided by operating activities	\$ <u>(17,247,820)</u>	\$ <u>8,643,844</u>

**Supplemental disclosure of non-cash capital financing activities**

Supplemental disclosure of non-cash capital financing activities		
Cost of construction of building and acquisition of equipment	\$ 3,521,289	\$ 1,818,240
Less: Accounts payable	-	(92,670)
Plus: Payment of short-term trade accounts used to finance construction of a building	<u>92,670</u>	<u>-</u>
Payment for construction of building and acquisition of equipment	\$ <u>3,613,959</u>	\$ <u>1,725,570</u>

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The accompanying notes are an integral part of these consolidated financial statements.

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### Nature of Operations

Local Government Center, Inc. (LGC) oversees the operations of its subsidiaries: Local Government Center HealthTrust, LLC (HealthTrust); Local Government Center Property-Liability Trust, LLC (Property-Liability Trust); New Hampshire Municipal Association, LLC (NHMA); and Local Government Center Real Estate, Inc. (Real Estate). LGC provides various programs and services to its members, who are governments and municipalities of the State of New Hampshire. Such programs are designed to serve the members by being a catalyst for dialogue and action, an advocate on issues, an advisor on programs, a provider of benefits and risk management services, an educator and trainer in skills, and a resource for information.

HealthTrust provides health coverage and related benefits to its members. Property-Liability Trust provides property-liability and workers' compensation coverage and risk management services to its members. NHMA's services include providing information and technical advice on municipal problems and issues, including legislative policy development and advocacy. Real Estate leases real estate to LGC and its subsidiaries and a third party.

As of December 31, 2009 and 2008, membership in the property and liability risk management component of Property-Liability Trust amounted to 361 and 350, respectively. As of December 31, 2009 and 2008, membership in the workers' compensation component amounted to 229 and 215, respectively. LGC HealthTrust's membership by product at December 31, 2009 and 2008 was as follows:

	<u>2009</u>	<u>2008</u>
Indemnity	5,441	6,010
POS	26,995	26,157
HMO	24,061	23,186
Medicare Supplemental	5,220	4,880
Dental	54,144	56,666
Prescription only	39,889	40,303
Short-term disability	2,912	2,804

### 1. Summary of Significant Accounting Policies

#### Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the authoritative standard-setting body for the establishment of governmental accounting and financial reporting principles. LGC's consolidated financial statements are presented using the economic resources measurement focus and the accrual basis of accounting.

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### **Accounting Standards**

Pursuant to GASB Statements No. 20, "Accounting and Financial Reporting for Proprietary Funds," and No. 29, "Other Governmental Entities That Use Proprietary Fund Accounting," LGC has elected to apply the provision of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

### **Principles of Consolidation**

The consolidated financial statements include the accounts of LGC and its wholly-owned subsidiaries. Significant intercompany transactions and balances have been eliminated in consolidation.

### **Use of Estimates**

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

### **Cash Equivalents**

Cash equivalents consist of all highly liquid investments with an original maturity of three months or less.

### **Investment Securities**

Investment securities consist of U.S. Government Sponsored Enterprise Securities, U.S. Treasury notes, corporate notes and municipal obligations, certificates of deposit, and mutual funds. The securities are carried in the financial statements at fair value. Fair value is determined based upon quoted market prices.

### **Investment in External Investment Pool**

HealthTrust and Property-Liability Trust maintain an equity position in an external investment pool sponsored by a government entity, which is carried at fair value. Fair value is determined by each entity's proportionate share of the total fair value of the underlying investment pool's portfolio.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

**Member Contributions**

Contributions are generally recognized as revenue on a monthly basis over the participation contract term. The portion of the contributions received in cash that will be earned in the future is deferred and reported as unearned contributions. Accounts and contributions receivable are stated at the amount management expects to collect from outstanding balances. Management considers all accounts and contributions receivable to be collectible; accordingly, an allowance for doubtful accounts has not been provided.

**Reinsurance**

LGC uses reinsurance agreements to reduce its exposure to large losses on all types of covered claims. Reinsurance permits recovery of a portion of losses from reinsurers, although it does not discharge LGC's primary liability of the risks reinsured. LGC does not report reinsured risks as liabilities unless it is probable that those risks will not be covered by reinsurers.

**Property and Equipment**

Property and equipment with an estimated useful life greater than one year is recorded at cost. The cost of maintenance and repairs is charged to expense as incurred, while renewals and betterments are capitalized. Upon sale or other disposition of assets, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in income.

Property and equipment is depreciated using primarily the straight-line method over the following useful lives:

	<u>Estimated Useful Lives (Years)</u>
Land improvements	15
Building and building improvements	31-40
Computer equipment	3-5
Office equipment	3-5
Vehicles	3

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### Claims Reserves

LGC establishes claims reserves based on estimates of the ultimate cost of claims (including future claim adjustment expenses) that have been reported, but not settled, and of claims that have been incurred, but not reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claims reserves does not necessarily result in an exact amount. Claims reserves are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and societal factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims reserves are charged or credited to expense in the periods in which they are made.

### Income Taxes

The income of LGC is exempt from federal and state income taxes under provisions of the Internal Revenue Code and State Statutes.

### Operating Revenues and Expenses

Principal operating revenues are charges to participating members for contributions to cover estimated benefit obligations and administrative costs. Principal operating expenses include claims incurred, underwriting and claims payment services, administrative expenses and depreciation of capital assets. Other income and expenses are classified as nonoperating in the financial statements.

## 2. Cash and Cash Equivalents

The Company maintains its cash in bank deposits and cash management accounts that are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 as of December 31, 2009 and up to \$250,000 as of December 31, 2008, or collateralized with securities held in joint custody with the bank. As of December 31, 2009 and 2008, the carrying amount of cash held, in total, in excess of the FDIC limit was approximately \$49,500,000 and \$65,500,000, respectively. The balance is collateralized with securities held in joint custody with the bank.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

**3. Investment Securities**

Investment securities insured or registered consist of:

	<u>2009</u>			
	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
U.S. Government Sponsored				
Enterprise Securities	\$ 20,204,347	\$ 720,334	\$ (77,405)	\$ 20,847,276
U.S. Treasury Notes	12,470,680	197,397	(55,634)	12,612,443
Corporate Notes	29,137,832	984,025	(695,162)	29,426,695
Municipal Obligations	1,459,372	26,868	(6,205)	1,480,035
Certificates of Deposit	12,027,881	-	-	12,027,881
Mutual Funds	<u>10,305,161</u>	<u>-</u>	<u>(1,125,807)</u>	<u>9,179,354</u>
Total	<u>\$ 85,605,273</u>	<u>\$ 1,928,624</u>	<u>\$ (1,960,213)</u>	<u>\$ 85,573,684</u>

	<u>2008</u>			
	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
U.S. Government Sponsored				
Enterprise Securities	\$ 19,705,734	\$ 915,638	\$ -	\$ 20,621,372
U.S. Treasury Notes	13,500,452	696,833	-	14,197,285
Corporate Notes	28,639,625	135,197	(3,074,762)	25,700,060
Municipal Obligations	809,813	16,407	(1,695)	824,525
Certificates of Deposit	24,258,236	-	-	24,258,236
Mutual Funds	<u>10,305,161</u>	<u>-</u>	<u>(2,983,989)</u>	<u>7,321,172</u>
Total	<u>\$ 97,219,021</u>	<u>\$ 1,764,075</u>	<u>\$ (6,060,446)</u>	<u>\$ 92,922,650</u>

The following table presents the fair value of investments held that represent 5% or more of LGC's total investments.

	<u>2009</u>	<u>2008</u>
Vanguard 500 Index Fund	\$ 6,777,838	\$ 5,485,636
.25% Certificate of Deposit, due June 1, 2010	7,018,913	N/A
.25% Certificate of Deposit, due May 3, 2010	5,008,968	N/A
2.34% Certificate of Deposit, due May 6, 2009	N/A	22,235,680

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

During 2009 and 2008, LGC realized a net gain of \$226,632 and \$205,013, respectively, from the sale of investment securities. The calculation of the realized gains and losses is independent of a calculation of the net change in the fair value of investment securities. Realized gains and losses on investment securities that have been held in more than one fiscal year and sold in the current year may have been recognized as an increase or decrease in the fair value of investment securities reported in the prior year.

### Custodial Credit Risk

Custodial credit risk for the certificates of deposit is the amount maintained in certificates of deposit that are in excess of the FDIC limit of \$250,000. As of December 31, 2009 and 2008, the amount of certificates of deposit held subject to custodial credit risk was approximately \$12,000,000 and \$24,300,000, respectively. These amounts were collateralized with securities held in joint custody with the bank.

For other investments, custodial credit risk is the risk that, in the event of failure of the counterparty, LGC will not be able to recover the value of its investments that are in the possession of the outside party. At December 31, 2009, LGC did not have any other investments subject to custodial credit risk.

### Interest Rate Risk

Interest rate risk is the risk that changes in market 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 market interest rates. LGC mitigates the risk that the market value of securities will fall due to changes in general interest rates by structuring the portfolio so securities mature to meet the cash requirements for ongoing operations, thus avoiding the need to sell securities on the open market prior to maturity.

The cost and fair value of investment securities at December 31, 2009 and 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

<u>Maturity Dates</u>	<u>2009</u>		<u>2008</u>	
	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>Amortized Cost</u>	<u>Fair Value</u>
Not applicable	\$ 10,305,161	\$ 9,179,354	\$ 10,305,161	\$ 7,321,172
Within 1 year	17,151,733	17,260,349	27,027,911	27,019,913
1-5 years	29,317,288	30,148,095	30,740,108	30,564,790
5-10 years	12,011,209	12,382,111	8,614,744	8,561,116
10+ years	<u>16,819,882</u>	<u>16,603,775</u>	<u>20,531,097</u>	<u>19,455,659</u>
Total	<u>\$ 85,605,273</u>	<u>\$ 85,573,684</u>	<u>\$ 97,219,021</u>	<u>\$ 92,922,650</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

Credit Risk

LGC's investment policy mitigates credit risk by limiting investments to the safest types of securities and diversifying the portfolio. As of December 31, 2009, LGC's investments were rated as follows:

<u>Investments</u>	<u>Rating</u>	<u>Rating Organization</u>	<u>Fair Value</u>
Corporate Notes	A1	Moody's	\$ 3,101,875
Corporate Notes	A2	Moody's	4,621,704
Corporate Notes	A3	Moody's	5,177,701
Corporate Notes	Aa1	Moody's	165,336
Corporate Notes	Aa2	Moody's	764,284
Corporate Notes	Aa3	Moody's	1,693,896
Corporate Notes	Aaa	Moody's/S&P	7,145,729
Corporate Notes	B1	Moody's	338,791
Corporate Notes	Ba2	Moody's	350,365
Corporate Notes	Baa1	Moody's	2,233,653
Corporate Notes	Baa2	Moody's	2,393,091
Corporate Notes	Baa3	Moody's	934,198
Corporate Notes	Caa2	Moody's	506,072
Certificate of Deposit	NR	NR	12,027,881
Municipal Obligations	A1	Moody's	799,875
Municipal Obligations	A3	Moody's	125,161
Municipal Obligations	Aa2	Moody's	297,037
Municipal Obligations	Aaa	Moody's	257,962
Mutual Funds	3 stars	Morningstar	9,179,354
U.S. Treasury Notes	Aaa	Moody's	12,612,443
U.S. Government Sponsored Enterprises:			
FNMA	Aaa	Moody's	9,225,983
GNMA	Aaa	Moody's	1,770,337
FHLMC	Aaa	Moody's	3,973,887
Other Agencies	Aaa	Moody's	<u>5,877,069</u>
Total			\$ <u><u>85,573,684</u></u>

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### 4. Investment in External Investment Pool

The investment in external investment pool represents HealthTrust's and Property-Liability Trust's share of the New Hampshire Public Deposit Investment Pool (NHPDIP), which is reported at fair value. NHPDIP was established under State of New Hampshire Statute, RSA 383:24. The Bank Commissioner, in conjunction with its Advisory Committee, provides regulatory oversight of the investment pool's operations.

### 5. Restricted Cash

Restricted cash represents funds set aside by Property-Liability Trust, under agreement with the State of New Hampshire for purposes of funding the surety bond requirement as mandated by the State with respect to the workers' compensation program.

### 6. Property and Equipment

Property and equipment consists of the following:

	<u>Year Ended December 31, 2009</u>			
	<u>Beginning</u> <u>Balance</u>	<u>Additions</u>	<u>Disposals</u>	<u>Ending</u> <u>Balance</u>
Land and land improvements	\$ 2,269,747	\$ 3,242	\$ -	\$ 2,272,989
Buildings and building improvements	5,242,800	2,073,814	-	7,316,614
Computer equipment	2,893,485	1,322,604	-	4,216,089
Office equipment	481,591	121,629	-	603,220
Vehicles	<u>78,502</u>	<u>-</u>	<u>(20,275)</u>	<u>58,227</u>
	10,966,125	3,521,289	(20,275)	14,467,139
Less accumulated depreciation	<u>2,518,034</u>	<u>558,684</u>	<u>(20,275)</u>	<u>3,056,443</u>
	<u>\$ 8,448,091</u>	<u>\$ 2,962,605</u>	<u>\$ -</u>	<u>\$11,410,696</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

	Year Ended December 31, 2008			
	Beginning Balance	Additions	Disposals	Ending Balance
Land and land improvements	\$ 2,215,628	\$ 54,119	\$ -	\$ 2,269,747
Buildings and building improvements	4,321,682	921,118	-	5,242,800
Computer equipment	3,555,430	836,187	(1,498,132)	2,893,485
Office equipment	526,646	6,816	(51,871)	481,591
Vehicles	<u>78,502</u>	<u>-</u>	<u>-</u>	<u>78,502</u>
	10,697,888	1,818,240	(1,550,003)	10,966,125
Less accumulated depreciation	<u>3,708,155</u>	<u>359,882</u>	<u>(1,550,003)</u>	<u>2,518,034</u>
	<u>\$ 6,989,733</u>	<u>\$ 1,458,358</u>	<u>\$ -</u>	<u>\$ 8,448,091</u>

**7. Premium Deficiency**

In accordance with GASB Statement No. 30, "Risk Financing Omnibus", premium deficiencies are required to be calculated and reported by public entity risk pools. Investment income was included as part of the calculation in determining if a premium deficiency existed. LGC determined that there were no premium deficiencies for any of the programs of HealthTrust and Property-Liability Trust at December 31, 2009 and 2008, respectively

The Parent's Board of Directors regularly evaluates net asset balances. Member rates are either increased to help protect members from periods of unanticipated claims volume or decreased in order to return undesignated net assets to members. Due to the level of net assets at the end of 2007, the LGC Board of Directors decided to adjust rates to return undesignated net assets to Members over an anticipated three-year period. During 2008 and 2009, rates included an amount of undesignated net assets as a rate credit. The amount of the return is adjusted based on the balance in unrestricted net assets at each year-end.

The operating losses for the workers' compensation and unemployment programs of Property-Liability Trust are mitigated by the continued support of LGC's Board of Directors. During the years ended December 31, 2009 and 2008, the Board of Local Government Center authorized contributions to Property-Liability Trust of \$3,928,371 and \$2,768,304, respectively, to support the operations of the Property-Liability Trust programs.

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### 8. Board Designated Net Assets

Board designated net assets includes the following at December 31, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
Pool risk management reserves for HealthTrust and Property-Liability Trust	\$ 78,492,313	\$ 66,651,686
Capital asset additions for Real Estate	-	2,769,757
Administrative needs for HealthTrust	<u>8,732,451</u>	<u>7,228,794</u>
	<u>\$ 87,224,764</u>	<u>\$ 76,650,237</u>

### 9. Self-Funded Plus Program

HealthTrust provides a claim servicing pool arrangement to certain participating members where separate accounts are maintained for each member from which losses are paid. Members are assessed fees by HealthTrust for the claims administrative services provided. The net activity from the program is recorded as part of operating revenues in the statement of revenues, expenses, and changes in net assets.

### 10. Exemption from Statutory Accounting Practices

LGC and its pooled risk management programs were established for the benefit of the political subdivisions of the State of New Hampshire under Title 1, Chapter 5-B of the New Hampshire statutes. As such, LGC is not considered an insurer under the laws of the State, and administration of the activities of LGC shall not constitute conducting an insurance business for purposes of regulation or taxation. At December 31, 2009, Statements of Statutory Accounting Practices as promulgated by the National Association of Insurance Commissioners are not applicable to LGC.

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### 11. Claims Reserves

LGC establishes a liability for both reported and unreported covered events, which includes estimates of both future payments of losses and related claim adjustment expenses, both allocated and unallocated. The following represents changes in those aggregate undiscounted liabilities for LGC during the years ended December 31, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
Claims reserves at beginning of year	\$ <b>42,976,498</b>	\$ 39,785,207
Incurred claims and claim adjustment expenses		
Provision for covered events of current year	<b>377,311,644</b>	331,936,106
Adjustments to provision for covered events of prior years	<u>(7,996,737)</u>	<u>(10,554,283)</u>
Total incurred claims and claim adjustment expenses	<u><b>369,314,907</b></u>	<u>321,381,823</u>
Payments of claims and claims adjustment expenses		
Payments attributable to covered events of current year	<b>(343,161,381)</b>	(299,061,672)
Payments attributable to covered events of prior years	<u>(22,373,502)</u>	<u>(19,128,860)</u>
Total payments	<u><b>(365,534,883)</b></u>	<u>(318,190,532)</u>
Total claims reserves at end of year	<u><b>\$ 46,756,522</b></u>	<u>\$ 42,976,498</u>

Incurred claims and claim adjustment expenses included in claims payable in the statements of financial position as of December 31, 2009 and 2008 are considered to have been paid for purpose of the claims reserves reconciliation as of and for the years ended December 31, 2009 and 2008.

### 12. Reinsurance Activity

LGC limits the maximum net loss that can arise from large risks by reinsuring (ceding) certain levels of risks with other insurers or reinsurers, through the purchase of excess loss reinsurance contracts. Ceded reinsurance is treated as the risk and liability of the assuming companies, though these reinsurance contracts do not relieve LGC from its obligations to participating members. Failure of reinsurers to honor their obligations could result in losses to LGC; consequently, allowances are established for amounts deemed uncollectible. LGC evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies.

For the workers' compensation coverage, Property-Liability Trust purchases specific excess insurance above a \$750,000 self-insured retention for all job classifications except for electric light or power companies for which it retains a \$2,000,000 retention. Prior to 2006, Property-Liability Trust obtained reinsurance for any single claim in excess of \$300,000 (\$500,000 for police and fire for the claim year after January 1, 2002).

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Effective July 1, 2008, Property-Liability Trust reinsurance coverage has been obtained for any single claim (specific insurance) has been obtained to cover liability losses in excess of \$1,000,000 and property losses in excess of \$500,000 for policy years ended after June 30, 2008; \$500,000 for 1997 to June 30, 2008; \$250,000 for 1994 to 1996; \$200,000 for 1990 to 1993; and \$150,000 for prior years. Coverage has also been obtained (for years prior to 1997) to cover losses that exceed a loss fund established in the reinsurance agreement. This aggregate reinsurance would cover an additional \$1,000,000 in claims should the entire loss fund be expended.

### 13. Leasing Arrangements

LGC leases automobiles under noncancellable operating leases expiring through December 2012. The future minimum lease payments required under the leases are as follows:

2010	\$	30,065
2011		27,067
2012		<u>8,549</u>
	\$	<u>65,681</u>

Rent expense under these leases totaled \$80,693 and \$87,967 for the years ended December 31, 2009 and 2008, respectively.

### 14. Description of Rent Agreements

Real Estate entered into a rent agreement with a third-party tenant (tenant A) during 2004. The initial term of the rent agreement is for a period of ten years, expiring on December 31, 2014. Beginning in April 2005, Real Estate provides office space to a third-party tenant (tenant B) at no charge for an initial term of ten years. The estimated fair value of the office space leased is approximately \$9,775 per year. The following is a schedule of future minimum lease payments to be received under the rent agreement with tenant A:

2010	\$	12,452
2011		12,452
2012		12,452
2013		12,452
2014		<u>12,452</u>
	\$	<u>62,260</u>

Rent income under the lease with tenant A totaled \$13,490 for 2009 and \$11,415 for 2008.

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

### **15. Deferred Compensation Plan**

The employees of LGC are covered by a Section 457 Deferred Compensation Plan administered by ICMA Retirement Corporation. All full-time employees are immediately eligible to participate in the plan and may elect to defer up to 100% of their gross compensation up to the federal limits. Employee contributions totaled \$265,318 and \$244,864 for the years ended December 31, 2009 and 2008, respectively. There were no employer contributions in 2009 and 2008.

### **16. Defined Benefit Pension Plan**

Effective January 1, 2007, LGC established the New Hampshire Local Government Center Defined Benefit Pension Plan (the Plan), a single employer plan. The LGC Board of Directors assigns the authority to establish, amend or terminate the Plan and its provisions at any time. The LGC Board of Directors also established a Retirement Committee to govern and administer the Plan. The Retirement Committee shall serve as the Plan Administrator to the Plan and shall have discretionary authority to interpret the terms of the Plan and its decisions regarding administration, interpretation, and application. All active employees of LGC are required to participate in the Plan as a condition of employment. The plan provides a monthly benefit when a Plan participant retires or leaves LGC after qualifying for benefits.

The contribution requirements of plan members and the LGC are established and may be amended by the LGC Board of Directors. A participant's benefit is determined under a formula that multiplies the participant's average monthly pay by her/his credited service with LGC. The formula is 1.50% of the final average salary (defined as the highest average of 3 Plan year's base salary out of the last 10 years prior to retirement or termination) for each year of credited service not to exceed 50% of the participant's average salary. If a participant chooses early retirement, the benefit will be reduced by 0.25% for each month prior to his normal retirement date. If a participant remains employed after age 65, benefits will continue to accrue without any actuarial adjustment for late retirement. The Plan does not issue a stand-alone financial report.

Participants shall contribute 5% of their earnings to the Plan. LGC shall contribute to the Plan an amount determined by its Board of Directors. For the years ended December 31, 2009 and 2008, LGC contributed 7.25% of each participant's earnings to the Plan. The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Investments are reported at fair value based upon quoted market prices.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

**SCHEDULE OF PLAN NET ASSETS AS OF DECEMBER 31, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
Cash and cash equivalents	\$ 47,030	\$ 932,350
Investments, at fair value	<u>4,855,323</u>	<u>2,337,686</u>
Net assets held in trust for pension benefits	\$ <u>4,902,353</u>	\$ <u>3,270,036</u>

**SCHEDULE OF CHANGES IN PLAN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
Contributions		
Employer	\$ 541,208	\$ 477,136
Plan members	<u>367,533</u>	<u>294,835</u>
Total contributions	<u>908,741</u>	<u>771,971</u>
Investment income (loss)		
Net realized and unrealized appreciation (depreciation) in fair value of investments	691,785	(945,116)
Interest	51,043	59,858
Dividends	40,387	43,142
Less investment fees	<u>(22,425)</u>	<u>(20,819)</u>
Net investment income (loss)	<u>760,790</u>	<u>(862,935)</u>
Benefits paid directly to participants	<u>(37,214)</u>	<u>(12,374)</u>
Net increase (decrease) in net assets held in trust for pension benefits	1,632,317	(103,338)
Net assets held in trust for pension benefits, beginning of year	<u>3,270,036</u>	<u>3,373,374</u>
Net assets held in trust for pension benefits, end of year	\$ <u>4,902,353</u>	\$ <u>3,270,036</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

LGC's annual pension cost and net pension obligation (asset) to the Plan as of and for the years ended December 31, 2009 and 2008 were:

	<u>2009</u>	<u>2008</u>
Annual required contribution	\$ <b>604,737</b>	\$ 454,399
Interest on net pension obligation	<u>(17,312)</u>	<u>(15,263)</u>
Annual pension cost	<b>587,425</b>	439,136
Less contributions made	<u>(541,208)</u>	<u>(477,136)</u>
Change in net pension obligation (asset)	<b>46,217</b>	(38,000)
Net pension obligation (asset), beginning of year	<u>(22,565)</u>	<u>15,435</u>
Net pension obligation (asset), end of year	\$ <u><b>23,652</b></u>	\$ <u>(22,565)</u>

Trend information is as follows:

<u>Plan year ended</u> <u>December 31,</u>	<u>Annual pension cost</u> <u>(APC)</u>	<u>Percentage of APC</u> <u>contributed</u>	<u>Net pension (asset)</u> <u>obligation</u>
2007	\$ 436,172	96.5 %	\$ 15,435
2008	439,136	108.7 %	(22,565)
<b>2009</b>	<b>587,425</b>	<b>92.1 %</b>	<b>23,652</b>

Additional information as of the latest actuarial valuation of January 1, 2009 is as follows:

Actuarial cost method	Aggregate actuarial cost method
	based on earnings
Asset valuation method	Market value
Actuarial assumptions	
Discount rate	6.5%
Section 417(e) interest rate	5.0%
Interest on employee contributions	4.0%
Projected salary increases	4.0%

# LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2009 and 2008

The funded ratio measures the relationship between valuation assets and the actuarial accrued liability. Information regarding the Plan's funded ratio as of the most recent valuation date is as follows:

Actuarial accrued liability	\$ 6,043,626
Actuarial value of plan assets	<u>3,270,036</u>
Unfunded actuarial accrued liability	\$ <u>2,773,590</u>
Funded ratio	54.1 %
Annual covered payroll	6,950,180
Unfunded actuarial accrued liability to annual covered payroll	39.9 %

The purpose of providing the above information is to provide information that approximates the funded status and funding progress of the plan.

### 17. Risks and Uncertainties

LGC invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect reported amounts in the consolidated financial statements.

### 18. Contingencies

LGC assesses potential liabilities in connection with lawsuits and threatened lawsuits under Financial Accounting Standards Board *Accounting Standards Codification* Topic 450, *Contingencies*. LGC accrues an estimated loss for loss contingencies if both of the following conditions are met: information available prior to issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of loss can be reasonably estimated. LGC expenses legal costs as they are incurred.

LGC and HealthTrust have received a Writ of Mandamus from the Professional Firefighters of New Hampshire demanding return of all excess earnings and surplus to participating local governments. The Board of Directors maintains these funds have been returned to participating local governments through rate credits and other means. The Board of Directors disputes the claims in the petition and is preparing a response to the petition. At this time, LGC believes there is no liability to recognize for this action.

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**December 31, 2009 and 2008**

Governor John Lynch signed HB 1393 into law on June 14, 2010. HB 1393 amends NH RSA 5-B by granting the Secretary of State the exclusive authority and jurisdiction over pooled risk management programs. Under HB 1393, the Secretary of State, in consultation with the insurance commissioner and by employing the services of an actuary who has experience with pooled risk management programs and is a qualified member of the American Academy of Actuaries, shall, no later than January 1, 2011, submit a report containing specific recommendations concerning the limitation of reserves in pooled risk management programs and the limitation of administrative expenses as a percentage of claims of pooled risk management programs. Until the report is submitted, the probability of the impact of HB 1393 on LGC cannot be determined nor can the nature of any limitations, if any, on reserves or administrative expenses, be estimated.

HealthTrust has contracted with certain of its members to provide them with assistance in applying to the Centers for Medicare and Medicaid Services (CMS) for Medicare Part D subsidy funds in connection with retiree prescription drug plans. In order to receive the Medicare Part D subsidy, LGC HealthTrust is required to file an application within a specified deadline. In prior years, CMS did not strictly enforce the filing deadline. A change in enforcement policy at CMS resulted in the denial of certain members' subsidy applications for the plan year ending June 30, 2009 on the basis that the application was filed a few days after the filing deadline. During 2009, LGC HealthTrust reimbursed members for the amount of the subsidy of approximately \$2 million.

## **SUPPLEMENTARY INFORMATION**

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Required Supplemental Information - Historical Pension Information  
(Unaudited)**

**December 31, 2009**

**Schedule of Funding Progress**

<u>Actuarial valuation date</u>	<u>Actuarial value of assets</u>	<u>Actuarial accrued liability (AAL)</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded ratio</u>	<u>Covered payroll</u>	<u>UAAL as a percentage of covered payroll</u>
1/01/09	\$ 3,270,036	\$ 6,043,626	\$ 2,773,590	54.1 %	\$ 6,950,180	39.9 %

**Schedule of Employer and Employee Contributions**

<u>Plan year ended December 31,</u>	<u>Annual required contributions</u>	<u>Employer contributions</u>	<u>Employee contributions</u>	<u>Percentage contributed</u>
2007	\$ 1,834,087	\$ 1,804,815	\$ 1,424,859	98.4 %
2008	454,399	477,136	294,835	105.0 %
<b>2009</b>	<b>604,737</b>	<b>541,208</b>	<b>367,533</b>	<b>89.5 %</b>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidating Schedule of Financial Position**

**December 31, 2009**

	<u>LGC, Inc.</u>	<u>Property- Liability Trust</u>	<u>HealthTrust</u>	<u>Real Estate</u>	<u>NHMA</u>	<u>Eliminations</u>	<u>Total</u>
Current assets							
Cash and cash equivalents	\$ 96,516	\$ 7,004,430	\$ 41,698,180	\$ 322,450	\$ 550,809	\$ -	\$ 49,672,385
Investment securities	-	28,552,741	57,020,943	-	-	-	85,573,684
Investment in external investment pool	-	6,593,553	5,936,168	-	-	-	12,529,721
Contributions receivable	-	415,395	4,903,985	-	-	-	5,319,380
Accounts receivable	28,450	-	3,835,230	-	-	-	3,863,680
Claims recovery receivable	-	46,458	-	-	-	-	46,458
Due from subsidiaries	300,055	-	-	-	-	(300,055)	-
Accrued interest receivable	-	254,378	323,849	-	-	-	578,227
Due from Parent	-	216,434	-	-	-	(216,434)	-
Prepaid expenses and deposits	<u>14,238</u>	<u>1,456,018</u>	<u>103,374</u>	<u>274</u>	<u>7,469</u>	<u>-</u>	<u>1,581,373</u>
Total current assets	439,259	44,539,407	113,821,729	322,724	558,278	(516,489)	159,164,908
Property and equipment, net	8,164	257,651	2,633,341	8,511,007	533	-	11,410,696
Restricted cash	-	1,000,000	-	-	-	-	1,000,000
Deposits	-	-	1,407,738	-	-	-	1,407,738
Investment in subsidiary	<u>9,294,522</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(9,294,522)</u>	<u>-</u>
Total assets	<u>\$ 9,741,945</u>	<u>\$ 45,797,058</u>	<u>\$ 117,862,808</u>	<u>\$ 8,833,731</u>	<u>\$ 558,811</u>	<u>\$ (9,811,011)</u>	<u>\$ 172,983,342</u>
Current liabilities							
Claims payable	\$ -	\$ -	\$ 11,372,830	\$ -	\$ -	\$ -	\$ 11,372,830
Claims reserves	-	23,171,413	23,585,109	-	-	-	46,756,522
Claims adjustments and administrative reserves	-	3,284,409	-	-	-	-	3,284,409
Accounts payable and accrued expenses	286,524	1,310,753	1,970,626	19,876	61,231	-	3,649,010
Deposits and other current liabilities	-	-	883,110	-	-	-	883,110
Retainage payable	-	-	-	-	-	-	-
Unearned contributions	5,100	8,125,580	245,884	-	71,825	-	8,448,389
Defined benefit obligation	23,652	-	-	-	-	-	23,652
Due to Parent	<u>-</u>	<u>59,183</u>	<u>323,677</u>	<u>38,616</u>	<u>95,013</u>	<u>(516,489)</u>	<u>-</u>
Total current and total liabilities	<u>315,276</u>	<u>35,951,338</u>	<u>38,381,236</u>	<u>58,492</u>	<u>228,069</u>	<u>(516,489)</u>	<u>74,417,922</u>
Net assets (deficit)							
Unrestricted	9,418,505	-	(756,875)	264,232	75,696	(9,294,522)	(292,964)
Board designated	-	9,339,725	77,885,039	-	-	-	87,224,764
Restricted	-	-	-	-	254,513	-	254,513
Invested in capital assets	8,164	257,651	2,633,341	8,511,007	533	-	11,410,696
Unrealized loss on investment securities	<u>-</u>	<u>248,344</u>	<u>(279,933)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(31,589)</u>
Total net assets	<u>9,426,669</u>	<u>9,845,720</u>	<u>79,481,572</u>	<u>8,775,239</u>	<u>330,742</u>	<u>(9,294,522)</u>	<u>98,565,420</u>
Total liabilities and net assets	<u>\$ 9,741,945</u>	<u>\$ 45,797,058</u>	<u>\$ 117,862,808</u>	<u>\$ 8,833,731</u>	<u>\$ 558,811</u>	<u>\$ (9,811,011)</u>	<u>\$ 172,983,342</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidating Schedule of Revenues, Expenses, and Changes in Net Assets**

**Year Ended December 31, 2009**

	<u>LGC, Inc.</u>	<u>Property- Liability Trust</u>	<u>HealthTrust</u>	<u>Real Estate</u>	<u>NHMA</u>	<u>Eliminations</u>	<u>Total</u>
Operating revenues							
Member contributions earned	\$ 662,643	\$ 19,064,924	\$ 368,673,579	\$ -	\$ 629,738	\$ -	\$ 389,030,884
Member contributions ceded	-	(3,355,822)	(2,182,257)	-	-	-	(5,538,079)
Self-funded plus program - net	-	-	(54,339)	-	-	-	(54,339)
Rent	-	-	-	316,480	-	(302,990)	13,490
Other revenue	<u>29,502</u>	<u>-</u>	<u>200,671</u>	<u>6,090</u>	<u>107,722</u>	<u>-</u>	<u>343,985</u>
Total net operating revenues	<u>692,145</u>	<u>15,709,102</u>	<u>366,637,654</u>	<u>322,570</u>	<u>737,460</u>	<u>(302,990)</u>	<u>383,795,941</u>
Operating expenses							
Claims incurred	-	16,482,999	352,831,908	-	-	-	369,314,907
Administrative fees	-	569,238	14,003,354	-	-	-	14,572,592
Other expenses	<u>1,646,847</u>	<u>6,012,167</u>	<u>14,071,198</u>	<u>565,726</u>	<u>628,133</u>	<u>(302,990)</u>	<u>22,621,081</u>
Total operating expenses	<u>1,646,847</u>	<u>23,064,404</u>	<u>380,906,460</u>	<u>565,726</u>	<u>628,133</u>	<u>(302,990)</u>	<u>406,508,580</u>
Operating (loss) income	(954,702)	(7,355,302)	(14,268,806)	(243,156)	109,327	-	(22,712,639)
Nonoperating income and expenses							
Investment income	669	1,279,284	2,442,880	1,575	356	-	3,724,764
Net increase in fair value of investment securities	-	1,303,288	2,961,493	-	-	-	4,264,781
Loss from subsidiary	(241,582)	-	-	-	-	241,582	-
Other income	<u>-</u>	<u>14,065</u>	<u>90,733</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>104,798</u>
(Decrease) increase in net assets before contributions and distributions	(1,195,615)	(4,758,665)	(8,773,700)	(241,581)	109,683	241,582	(14,618,296)
Transfers to Subsidiary	(3,928,371)	3,928,371	-	-	-	-	-
Transfers to Parent	<u>4,676,830</u>	<u>(246,057)</u>	<u>(4,430,773)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
(Decrease) increase in net assets	(447,156)	(1,076,351)	(13,204,473)	(241,581)	109,683	241,582	(14,618,296)
Net assets, beginning of year	<u>9,873,825</u>	<u>10,922,071</u>	<u>92,686,045</u>	<u>9,016,820</u>	<u>221,059</u>	<u>(9,536,104)</u>	<u>113,183,716</u>
Net assets, end of year	<u>\$ 9,426,669</u>	<u>\$ 9,845,720</u>	<u>\$ 79,481,572</u>	<u>\$ 8,775,239</u>	<u>\$ 330,742</u>	<u>\$ (9,294,522)</u>	<u>\$ 98,565,420</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidating Schedule of Cash Flows**

**Year Ended December 31, 2009**

	<u>LGC, Inc.</u>	<u>Property- Liability Trust</u>	<u>HealthTrust</u>	<u>Real Estate</u>	<u>NHMA</u>	<u>Eliminations</u>	<u>Total</u>
Cash flows from operating activities							
Member contributions collected	\$ 701,985	\$ 19,479,692	\$ 369,080,204	\$ -	\$ 636,569	\$ -	\$ 389,898,450
Member contributions ceded to reinsurer	-	(3,846,633)	(2,182,257)	-	-	-	(6,028,890)
Restricted contributions received	-	-	-	-	107,722	-	107,722
Rental income collected	-	-	-	316,480	-	(302,990)	13,490
Other revenue received	-	-	200,671	6,090	-	-	206,761
Employee and other expenses paid	(1,618,107)	(2,258,375)	(30,445,734)	(349,295)	(613,878)	302,990	(34,982,399)
Claims paid	-	(13,336,315)	(350,504,779)	-	-	-	(363,841,094)
Loss prevention expenses paid	-	(2,892,478)	-	-	-	-	(2,892,478)
Net cash provided by self-funded plus program	<u>-</u>	<u>-</u>	<u>270,618</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>270,618</u>
Net cash (used) provided by operating activities	<u>(916,122)</u>	<u>(2,854,109)</u>	<u>(13,581,277)</u>	<u>(26,725)</u>	<u>130,413</u>	<u>-</u>	<u>(17,247,820)</u>
Cash flows from investing activities							
Proceeds from the sale of investment securities	-	7,477,007	77,623,965	-	-	-	85,100,972
Interest and dividends on investment securities	669	1,367,078	2,399,274	1,575	356	-	3,768,952
Purchase of external investment pool	-	(3,986,712)	(5,507,327)	-	-	-	(9,494,039)
Purchase of investment securities	<u>-</u>	<u>(7,456,210)</u>	<u>(68,118,624)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(75,574,834)</u>
Net cash provided (used) by investing activities	<u>669</u>	<u>(2,598,837)</u>	<u>6,397,288</u>	<u>1,575</u>	<u>356</u>	<u>-</u>	<u>3,801,051</u>
Cash flows from capital and related financing activities							
Payment for construction of building and acquisition of capital assets	<u>(875)</u>	<u>(225,430)</u>	<u>(1,026,155)</u>	<u>(2,361,499)</u>	<u>-</u>	<u>-</u>	<u>(3,613,959)</u>
Net cash used by capital and related financing activities	<u>(875)</u>	<u>(225,430)</u>	<u>(1,026,155)</u>	<u>(2,361,499)</u>	<u>-</u>	<u>-</u>	<u>(3,613,959)</u>
Cash flows from noncapital financing activities							
Distributions to Parent	4,676,830	(246,057)	(4,430,773)	-	-	-	-
Cash received from other income	-	14,065	90,733	-	-	-	104,798
Contribution to net assets from Parent	<u>(3,834,506)</u>	<u>3,834,506</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net cash provided (used) by noncapital financing activities	<u>842,324</u>	<u>3,602,514</u>	<u>(4,340,040)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>104,798</u>
Net (decrease) increase in cash and cash equivalents	(74,004)	(2,075,862)	(12,550,184)	(2,386,649)	130,769	-	(16,955,930)
Cash and cash equivalents, beginning of year	<u>170,520</u>	<u>9,080,292</u>	<u>54,248,364</u>	<u>2,709,099</u>	<u>420,040</u>	<u>-</u>	<u>66,628,315</u>
Cash and cash equivalents, end of year	<u>\$ 96,516</u>	<u>\$ 7,004,430</u>	<u>\$ 41,698,180</u>	<u>\$ 322,450</u>	<u>\$ 550,809</u>	<u>\$ -</u>	<u>\$ 49,672,385</u>

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Consolidating Schedule of Cash Flows (Concluded)**

**Year Ended December 31, 2009**

	<u>LGC, Inc.</u>	<u>Property- Liability Trust</u>	<u>HealthTrust</u>	<u>Real Estate</u>	<u>NHMA</u>	<u>Eliminations</u>	<u>Total</u>
Reconciliation of operating (loss) income to net cash (used) provided by operating activities							
Operating (loss) income	\$ (954,702)	\$ (7,355,302)	\$ (14,268,806)	\$ (243,156)	\$ 109,327	\$ -	\$ (22,712,639)
Adjustments to reconcile operating (loss) income to net cash (used) provided by operating activities							
Depreciation and amortization	6,897	55,827	286,534	208,864	562	-	558,684
(Increase) decrease in							
Contributions receivable	11,175	34,459	614,177	-	-	-	659,811
Accounts receivable	-	-	666,390	-	-	-	666,390
Claims recovery receivable	-	55,820	-	-	-	-	55,820
Prepaid expenses and deposits	9,195	(362,038)	209,127	(17)	1,446	-	(142,287)
Increase (decrease) in							
Claims payable	-	-	1,670,003	-	-	-	1,670,003
Claims reserves	-	3,090,864	689,160	-	-	-	3,780,024
Claims adjustment reserves	-	1,607,409	-	-	-	-	1,607,409
Deposits held	-	-	(193,640)	-	-	-	(193,640)
Accounts payable and accrued expenses	(88,754)	(266,779)	(3,032,253)	(5,505)	10,050	-	(3,383,241)
Unearned contributions	(1,335)	380,309	(207,552)	-	(9,228)	-	162,194
Defined benefit obligation	23,652	-	-	-	-	-	23,652
Due to Parent and affiliates	<u>77,750</u>	<u>(94,678)</u>	<u>(14,417)</u>	<u>13,089</u>	<u>18,256</u>	<u>-</u>	<u>-</u>
Net cash (used) provided by operating activities	\$ <u>(916,122)</u>	\$ <u>(2,854,109)</u>	\$ <u>(13,581,277)</u>	\$ <u>(26,725)</u>	\$ <u>130,413</u>	\$ <u>-</u>	\$ <u>(17,247,820)</u>



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

Board of Directors  
Local Government Center, Inc. and Subsidiaries

We have audited the accompanying consolidated financial statements of Local Government Center, Inc. and Subsidiaries (LGC) as of and for the year ended December 31, 2009 and have issued our report thereon dated June 18, 2010. That report contained an explanatory paragraph addressing the omission of required supplementary information, including management's discussion and analysis. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered LGC's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of LGC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of LGC's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of LGC's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## Compliance and Other Matters

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

We noted certain matters that we reported to management of Local Government Center, Inc. in a separate letter dated June 18, 2010.

This report is intended solely for the information and use of the Board of Directors of Local Government Center, Inc. and management, and is not intended to be and should not be used by anyone other than these specified parties.



Manchester, New Hampshire  
June 18, 2010

**LOCAL GOVERNMENT CENTER, INC. AND SUBSIDIARIES**

**Summary Schedule of Prior Audit Findings**

**Year Ended December 31, 2009**

Finding Number: 2008-01

Condition Found: LGC HealthTrust contracts with member groups to provide assistance in applying to the Centers for Medicare and Medicaid Services ("CMS") in order to receive Medicare Part D subsidy funds in connection with the retiree prescription drug plans. In order to receive the Medicare Part D subsidy, LGC HealthTrust is required to file an application within a specified deadline. In prior years, we understand CMS did not strictly enforce the filing deadline. A change in enforcement policy at CMS resulted in the denial of certain members' subsidy applications for the plan year ending June 30, 2009 on the basis that the application was filed a few days after the filing deadline. LGC HealthTrust filed an appeal which is currently pending with CMS. If CMS denies that appeal, LGC HealthTrust expects to pay member groups the amount of the lost subsidy.

Recommendation: We recommend LGC HealthTrust file the Medicare Part D subsidy application within the filing deadline established by CMS.

Action Taken: LGC HealthTrust immediately took steps to mitigate the chance of this recurring. Two LGC HealthTrust individuals are designees for each Medicare D filing. A 30-day extension is promptly applied for and, instead of waiting for all other steps to be completed, LGC HealthTrust immediately produces and transmits the required information to the Medicare Part D Retiree Drug Subsidy Program. This provides LGC HealthTrust with sufficient time in order to be able to manage its portions of the application process. In addition, a tracking system has been established in a shared MS Excel worksheet to track the stages of each application. The Operations Manager maintains a MS Outlook Task List item to assure the timeliness of all applications being processed by LGC HealthTrust.

Status: **CORRECTED**