LOUISIANA INSURANCE GUARANTY ASSOCIATION

FINANCIAL STATEMENTS
(Cash Basis)

YEARS ENDED DECEMBER 31, 1999 AND 1998

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Independent Auditors' Report

Members and Directors
Louisiana Insurance Guaranty Association
Baton Rouge, Louisiana

We have audited the accompanying statements of financial position arising from cash transactions of Louisiana Insurance Guaranty Association as of December 31, 1999 and 1998, and the related statements of activities for the years then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing 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 audits 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 and disclosures 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 audits provide a reasonable basis for our opinion.

As described in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Louisiana Insurance Guaranty Association as of December 31, 1999 and 1998, and its changes in net assets during the years then ended, on the basis of accounting described in Note 1.

In accordance with Government Auditing Standards, we have also issued our report dated February 1, 2000 on our consideration of the Louisiana Insurance Guaranty Association's internal control over financial reporting and our tests of its compliance certain provisions of laws and regulations.

Since these financial statements are prepared on a cash basis, no liability is recorded for future payments for return of unearned premiums or claims. However, as discussed in Note 7 to the financial statements, the Association regularly estimates liabilities for such losses. These estimated losses have not been audited by us and accordingly we express no opinion or any other form of assurance on them.

Postlethwaite & Netterville

Baton Rouge, Louisiana
February 1, 2000

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF FINANCIAL POSITION
ARISING FROM CASH TRANSACTIONS
DECEMBER 31, 1999 AND 1998

ASSETS

	1999	1998
Cash	$ 33,833	$ 95,654
Investments	85,060,915	83,097,527
	$ 85,094,748	$ 83,193,181

LIABILITIES AND NET ASSETS

	1999	1998
Outstanding checks in excess of bank balances	$ 590,222	$ 828,866
Net Assets	84,504,526	82,364,315
	$ 85,094,748	$ 83,193,181

The accompanying notes are an integral part of these statements.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF ACTIVITIES
YEARS ENDED DECEMBER 31, 1999 AND 1998

	1999	1998
RECEIPTS		
Distributions from liquidators	$ 10,786,666	$ 24,169,428
Interest income	4,850,844	6,773,412
Net gain (loss) on sales of investments	(965,398)	266,181
Restitutions	195,795	174,302
Assessments received from members	126,180	-
Other receipts	2,364	320
	14,996,451	31,383,643
DISBURSEMENTS		
Claims paid	8,223,619	12,551,580
Unearned premiums paid	903	26,949
Legal fees and expenses	2,922,359	3,984,573
Claims handling costs	999,347	1,135,165
Professional and bank fees	165,415	251,903
Staff salaries, taxes, and benefits	324,567	318,579
Travel, meetings, and seminars	17,069	28,364
Administrative expenses	202,962	192,082
Interest expense	-	1,345,095
Loss on bond defeasement (Note 5)	-	348,529
Return of 1998 assessments collected in 1997	-	1,649,983
	12,856,241	21,832,802
EXCESS OF RECEIPTS OVER DISBURSEMENTS	2,140,211	9,550,841
Net Assets - beginning of the year	82,364,315	72,813,474
Net Assets - end of the year	$ 84,504,526	$ 82,364,315

The accompanying notes are an integral part of these statements.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

NOTES TO FINANCIAL STATEMENTS

1. **Significant Accounting Policies**

Organization

The Louisiana Insurance Guaranty Association (the Association) is an organization created by the Louisiana Insurance Guaranty Act to pay for the claims against insolvent member insurance companies. Funds are provided for the payment of the claims by the assessment of the remaining member insurance companies. All admitted insurance companies doing business in Louisiana except those writing life, health and accident, title, disability, mortgage guaranty, and ocean marine insurance as well as all types of reinsurance, are required to be members of the Association.

The Association has consolidated its operations and expanded its capabilities by establishing an in house Claims Unit to handle all claims processing. As of July 1999, all remaining workers' compensation claims were brought in-house with no remaining outside claims service providers. All administrative functions are performed by the Association's staff.

Accounting Method

The Association's policy is to prepare its financial statements on the basis of cash receipts and disbursements; consequently, revenue and related assets are recognized when received, and expenses and related liabilities are recognized when paid. Accordingly, no liabilities are recorded for future payments for unearned premiums, loss claims or related expenses. As discussed in Note 7, the Association regularly estimates liabilities for such liabilities.

Income Taxes

The Association is exempt from income taxes under Internal Revenue Code Section 501(c)(6); therefore, no provision for income taxes has been made.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

NOTES TO FINANCIAL STATEMENTS

2. **Investments**

The Association's investments are recorded at cost and consisted of the following at December 31, 1999 and 1998:

	1999		1998	
	Cost	Fair Value	Cost	Fair Value
U.S. Government securities under Agreement to sell	$ 626,553	$ 626,553	$ 273,000	$ 273,000
Money market accounts invested in U.S. Treasury obligations	2,808,835	2,808,835	13,059,749	13,105,125
U.S. Treasury notes and bonds	44,712,754	43,411,244	33,215,918	33,392,533
U.S. Government Agency obligations	36,912,773	36,226,333	36,548,860	36,730,939
	$ 85,060,915	$ 83,072,965	$ 83,097,527	$ 83,501,597

During 1998, the Association began to purchase individual securities issued by the U.S. Treasury and obligations issued or guaranteed by the U.S. Government and its Agencies. The fair value of these securities is based on quoted market prices. The Association enters into short-term repurchase agreements with Louisiana financial institutions whereby the Association purchases U.S. Government securities with an agreement to resell the securities to the financial institution at cost. The Association also deposits funds in money market funds invested in U.S. Treasury obligations.

During 1999, the Association realized unusual losses on its investment portfolio due to the trustee bank's failure to maintain compliance with established term to maturity guidelines. These losses are recorded net of restitution and will be offset by higher yields on conforming investments purchased by the successor trustee bank.

3. **Permanently Restricted Net Assets**

Net assets represent funds collected from member insurance companies in excess of funds disbursed to pay claims and expenses of the Association. All assets are considered permanently restricted under the Act creating the Association. Excess funds are to be used for the payment of claims, return of unearned premiums and reimbursement of expenses incurred for the insolvent member insurance companies (See Note 7). On December 17, 1998, the Association adopted a resolution to distribute $12 million of the net assets to the State of Louisiana pending further Board action.

NOTES TO FINANCIAL STATEMENTS

4. **Assessments**

Louisiana Revised Statute 22:1382 gives the Association the authority to assess member insurance companies the amount necessary to pay the obligations and expenses of the Association. Beginning January 1, 1990, and ending December 31, 2002, the assessment to member insurance companies cannot exceed an amount equal to two percent (2%) of net direct written premiums during the preceding calendar year. Beginning January 1, 2003, and thereafter, the assessment to member insurance companies is not to exceed an amount equal to one percent (1%) of net direct written premiums during the preceding calendar year, unless changed by the Louisiana Legislature.

The Association has determined that seven member companies qualify for earned credits of up to 80% of their annual assessments. Member companies can also qualify for assessment reductions by investing in qualifying Louisiana securities.

Pursuant to agreements entered into by the Association related to the issuance of bonds, see Note 5, the Association was obligated to assess member insurance companies the maximum permitted percentage of net direct written premiums each calendar year until these bonds and related obligations were paid in full or otherwise defeased. As discussed in Note 5, the Association defeased all outstanding bond obligations. On that date, the Association's Board of Directors reduced the 1998 assessment to one percent (1%) of each member insurer's net direct written premium during 1997. In December 1998, the Association's Board further reduced the 1998 assessment to zero and returned to members all amounts previously collected for 1998 assessments, including the return of $1,649,983 of 1998 assessments collected in 1997. For the year ended December 31, 1999, no assessments were made.

5. **Bonds Payable**

On October 25, 1993, the Association, in conjunction with the Louisiana Public Facilities Authority (LPFA), entered into certain trust, indentures, and other agreements whereby the Association issued LPFA Special Insurance Assessment Revenue Bonds Series 1993 dated October 1, 1993 in the amount of $136,705,000.

On February 2, 1998, the Association entered into an Escrow Deposit Agreement and deposited $93,126,046 into escrow trust accounts established to provide for the repayment of all scheduled bond maturities and related interest costs when due. By entering into these agreements and investing the escrow trust funds in securities issued by the U. S. Treasury, which are restricted only for the repayment of the bonds and related costs, the Association's outstanding bond obligations at that date of $92,035,000 were considered defeased. Accordingly, these bonds and investments held in trust, as well as all related interest income and expense are not reflected in the Association's financial statements. At December 31, 1999 and 1998, the bond escrow trust investments consist of State and Local Government Series securities issued by the U.S. Treasury with a cost of approximately $57,680,000 and $75,700,400. These investments, as well as the defeased bonds outstanding of $58,405,000 and $75,705,000 at December 31, 1999 and 1998, are not reflected in the Association's financial statements.

6. **Early Access Distributions by Liquidators**

The Association files claims against the estates of insolvent insurers in an effort to recover a portion of the policyholder claims paid and related expenses from the assets of the insolvent insurer. During the years ended December 31, 1999 and 1998, the Association received $10,786,666 and $24,169,428, respectively, of such distributions which are reflected as receipts in these financial statements. No estimate is available of future potential distributions from liquidations due to the uncertainty and difficulty in accurately estimating these amounts.

7. **Estimate of Future Return of Unearned Premiums and Claims Payments** (Not Audited)

The funds of the Association are used to pay insurance claims of insolvent member insurance companies (See Note 3). These claims are pursuant to the Louisiana Insurance Guaranty Law, LA. R.S. 22:1375-1394. As of December 31, 1999, the Association had 1,965 open claims files outstanding, a substantial portion of which are involved in litigation. Additionally, other member insurance companies may be declared insolvent subsequent to the date of these financial statements.

Due to the uncertainty involved in accepting and administering insolvent companies, as well as the difficulty in determining reliable estimates, the Association maintains its financial records on a cash basis. However, the Association regularly attempts to estimates the amount of claims and claims administration expenses related to insolvent member insurance companies as a function of managing and administering those losses.

Provided on the next page is an unaudited condensed balance sheet of the Association at December 31, 1999, on a modified accrual basis which recognizes management's estimate of claims and related liabilities, assessments received in advance, and accruals of interest. This information is intended to reflect only certain estimated assets and liabilities of the Association and is not intended to represent the financial position of the Association in accordance with generally accepted accounting principles. These estimates are expected to vary as additional information becomes available.

The condensed unaudited balance sheet does not provide for accruals of amounts due from liquidators of insolvent insurance companies, adjustments of investments to estimated fair value, and accruals of operating costs owed at year end not included in the reserves for claims administration expenses.

As described in Note 4, the Association has been granted the authority to assess member insurers at a rate of two percent (2%) which is expected to produce approximately $82 million annually. Additionally, LA R.S. 22:1382 provides that if the maximum assessment and other assets available to the Association are insufficient to make all necessary payments, the Association may borrow additional funds or payments can be reduced on a prorated basis and unpaid balances are to be paid as funds become available.

7. **Estimate of Future Return of Unearned Premiums and Claims Payments** (Not Audited) (continued)

ASSETS

	December 31, 1999 Unaudited
Cash	$ 33,833
Investments, at cost	85,060,915
Accrued interest receivable	1,195,680
Total assets	$ 86,290,428

LIABILITIES AND NET ASSETS

Outstanding checks in excess of bank balances	$ 590,222	
Estimated claims and claims administration expenses payable	60,504,500	(1)
Total liabilities		
Net assets	25,195,706	(2)
Total liabilities and net assets	$ 86,290,428	

(1)Represents management's estimate of claims and claims administration expense reserves related to open claim files at December 31, 1999. Management estimates that these claims and expenses should become due and be paid over a projected five year period.

The Association has recently been notified of several claims, as well as threatened claims, by certain large insureds of insolvent insurance companies relating to the use and production of asbestos, silica, tobacco, and environmentally hazardous materials. The Association is currently evaluating the merits of these claims, the appropriateness of coverage under the Act, and the amount of potential liability to the Association.

Management and legal counsel believe it to be premature to assess the likelihood or extent that any or all of these types of claims may ultimately be covered by the Association due to the numerous uncertainties related to the assertions of these claims. Management has been unable to estimate with any degree of reasonable certainty the amount of possible costs or liabilities the Association could be obligated to incur for such claims. For these reasons management has not included any estimated costs for claims made or threatened by large insureds in the above estimated claims liabilities. As facts and circumstances develop, management intends to

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7. **Estimate of Future Return of Unearned Premiums and Claims Payments** (Not Audited) (continued)

develop estimates and record estimated claims liabilities, if necessary, for claims made by large insureds. If these recently asserted claims are ultimately determined to be covered by the Act, the ultimate cost to settle these contingent liabilities could be substantial to the Association.

(2)The Association projects that the receipt of investment earnings and the continued receipt of proceeds from liquidators of insolvent insurance companies should be sufficient to satisfy the Association's estimated claims obligations as they become due. As described in Note 4, the Association may also increase the annual assessment rate, up to 2% of direct written premiums, if necessary to pay its obligations.

8. **Lease Commitment**

The Association has entered into operating leases for office space for which the Association paid $124,137 and $131,218 during the years ended December 31, 1999 and 1998, respectively. The following is a schedule, by year, of the minimum future lease obligations under these leases as of December 31, 1999.

Years Ending December 31,	
2000	$ 116,010
2001	117,164
2002	120,628
2003	122,987
2004	81,958
	$ 558,749

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Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Directors
Louisiana Insurance Guaranty Association
Baton Rouge, Louisiana

We have audited the financial statements of Louisiana Insurance Guaranty Association as of and for the year ended December 31, 1999, and have issued our report there on dated February 1, 2000. We conducted our audit in accordance with 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.

Compliance
As part of obtaining reasonable assurance about whether Louisiana Insurance Guaranty Association's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting
In planning and performing our audit, we considered Louisiana Insurance Guaranty Association's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board of Directors, management of the Louisiana Insurance Guaranty Association, the Commissioner of Insurance, the State of Louisiana, and the Legislative Auditor, State of Louisiana and is not intended to be and should not be used by anyone other than these specified parties.

Postlethwaite & Netterville

February 1, 2000

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