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LOUISIANA INSURANCE GUARANTY ASSOCIATION

FINANCIAL STATEMENTS
(Cash Basis)

YEARS ENDED DECEMBER 31, 1997 AND 1996

Under provisions of state law, this report is a public document. A copy of the report has been submitted to the audited, or reviewed, entity and other appropriate public officials. The report is available for public inspection at the Baton Rouge office of the Legislative Auditor and, where appropriate, at the office of the parish clerk of court.

Release Date 4-22-98

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LOUISIANA INSURANCE GUARANTY ASSOCIATION

FINANCIAL STATEMENTS
(Cash Basis)

YEARS ENDED DECEMBER 31, 1997 AND 1996

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Postlethwaite & Netterville

A Professional Accounting Corporation

CERTIFIED PUBLIC ACCOUNTANTS

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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, 1997 and 1996, 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, 1997 and 1996, 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 March 17, 1998 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
March 17, 1998

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ASSOCIATED OFFICES IN PRINCIPAL CITIES OF THE UNITED STATES

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF POSITION
ARISING FROM CASH TRANSACTIONS
DECEMBER 31, 1997 AND 1996

ASSETS

	1997	1996
Cash	$ 1,502,400	$ 72,095
Investments	164,011,882	114,490,379
	$ 165,514,282	$ 114,562,474

LIABILITIES AND NET ASSETS

Outstanding checks in excess of bank balances	$ 1,268,432	$ 1,786,883
Bonds payable	91,432,376	106,862,376
	92,700,808	108,649,259
Net Assets	72,813,474	5,913,215
	$ 165,514,282	$ 114,562,474

The accompanying notes are an integral part of these statements.

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LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF ACTIVITIES
YEARS ENDED DECEMBER 31, 1997 AND 1996

	1997	1996
RECEIPTS		
Assessments received from members	$ 76,588,108	$ 72,117,829
Early access distributions by liquidators	6,679,558	16,850,380
Interest income	7,375,198	5,390,116
Other receipts	106,983	77,336
	90 749 847	94,435,661
DISBURSEMENTS		
Loss claims	12,534,838	20,517,403
Premiums returned	712,863	521,460
Legal fees and claims handling expenses reimbursed to attorneys	3,998,218	6,329,116
Management and administrative fees	648,330	2,233,005
Claims handling fees to outside adjusters	350,280	428,340
Claims handling expenses reimbursed to servicing agencies	158,965	161,223
Claims handling fees and expenses - in house	509,885	109,159
Interest expense	4,488,075	5,056,305
Administrative staff expense	327,482	378,056
Computer equipment and software	-	152,471
Trust and bank fees	14,043	14,997
Miscellaneous	106,609	112,056
	23,849,588	36,013,591
EXCESS OF RECEIPTS OVER DISBURSEMENTS	66,900,259	58,422,070
Net Assets - beginning of the year	5,913,215	(52,508,855)
Net Assets - end of the year	$ 72,813,474	$ 5,913,215

The accompanying notes are an integral part of these statements.

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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, except workers' compensation claims. Workers' compensation claims continue to be processed by the Association's one remaining outside claims service provider. 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.

Lease Commitment

The Association has entered into operating leases for office space for which the Association paid $125,446 and $71,145 during the years ended December 31, 1997 and 1996, respectively. These leases require future minimum payments of $127,408 in 1998 and $42,996 in 1999.

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LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

NOTES TO FINANCIAL STATEMENTS

2. **Investments**

Bond indentures require that funds be invested in interest-bearing investments which are recorded at cost. 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. The market value of the repurchase agreements and money market accounts approximates cost. Investments in collateral investment contracts represent U. S. Treasury securities owned by the Association and repurchase agreements entered into with Westdeutsche Landesbank Girozentrale, New York Branch (WLG) whereby WLG agrees to repurchase the U. S. Treasury securities at an amount not less than the purchase price and to yield 4.3% or 4.96%, depending on the contract. Investments in collateral investment contracts are agreements between specific entities with guaranteed interest rates over the life of the respective bond issues and have no secondary market. Therefore, the market value is considered the same as cost.

Substantially all investments are restricted for debt service on the bonds and are as follows:

	1997	1996
U. S. Government securities under agreement to sell	$ 442,000	$ 3,159,000
Money market accounts invested in U. S. Treasury obligations	126,125,452	71,150,057
Collateral Investment Contract with Westdeutsche Landesbank Girozentrale, New York Branch	37,444,430	40,181,322
	$ 164,011,882	$ 114,490,379

At December 31, 1997 and 1996, $13,670,406 and $13,670,500 of the collateral investment contract investments were held in a restricted trust account as security for the bonds and were unavailable for operations. As described in Note 5, a significant amount of the Association's investments were used on February 2, 1998 to defease bonds outstanding.

3. **Permanently Restricted Net Assets (Deficit)**

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).

Pursuant to a plan of rehabilitation of Bonneville Insurance Company, the Association received $135,000 during 1996. The Association paid claims and related expenses of $53,335 and $35,058 during 1997 and 1996, respectively, from these funds. At December 31, 1997 and 1996, $358,077 and $392,597, respectively, of the Association's investments were held in trust and restricted to the payment of claims pursuant to Bonneville Insurance Company. The Association estimates that substantially all of these funds will be expended for claims and any remaining funds will be returned pursuant to this plan of rehabilitation.

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.

5. **Bonds Payable**

During the year ended December 31, 1990, the Association, in conjunction with the Louisiana Public Facilities Authority (LPFA), entered into certain trust, indenture and other agreements whereby the Association issued LPFA Special Insurance Assessment Revenue Bonds Series 1990 not to exceed $50 million. These bonds were refunded on October 25, 1993 and all security and related agreements were terminated.

On October 25, 1993, the Association, again in conjunction with the Louisiana Public Facilities Authority, 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. The net bond proceeds (after payment of $1,384,000 in underwriting and bond issuance costs) were used to refund the Series 1990 bonds and will be used to pay covered claims to claimants or policyholders arising through the insolvency of member insurance companies and to establish various reserve funds as required by the related bond trust indentures.

The Series 1993 bonds and accrued interest thereon were secured by substantially all of the assets of the Association, assessments received and receivable, and an insurance policy issued by Financial Security Assurance, Inc. The bonds do not constitute or create, in any way, an obligation of the State of Louisiana or any political subdivision thereof.

The Series 1993 bonds outstanding bear interest at rates ranging from 3.90% to 4.60% (effective average interest rate of 4.539% for term of bonds) which is payable semi-annually on each April 1 and October 1. At December 31, 1997 and 1996, there was approximately $1,008,822 and $1,159,300, respectively, of accrued interest owed on the bonds. Certain of the Series 1993 bonds were sold with an original issue discount of $602,624 which is shown as a reduction of the outstanding principal for the bonds.

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 schedules 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 are considered defeased.

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, 1997 and 1996, the Association received $6,679,558 and $16,850,380, 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, 1997, the Association had 3,830 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, 1997, 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, the deferral of financing costs related to the bond issuances, and accruals of operating costs owed at year end and 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 $78 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, 1997 Unaudited
Cash	$ 1,502,400
Investments	164,011,882
Accrued interest receivable	1,234,000
Total assets	$ 166,748,282

LIABILITIES AND NET ASSETS (DEFICIT)

Outstanding checks in excess of bank balances	$ 1,268,432	
Estimated claims and claims administration expenses payable	81,832,985	(1)
Assessments received in advance	1,649,982	
Accrued interest payable and other expenses	1,008,832	
Bonds payable	91,432,376	(2)
Total liabilities	177,192,607	
Net assets (deficit)	(10,444,325)	(3)
Total liabilities and net assets (deficit)	$ 166,748,282	

(1) Represents management's estimate of claims and claims administration expense reserves related to open claim files at December 31, 1997. Management estimates that these claims and expenses should become due and be paid over a projected five year period.

(2) The bonds were defeased on February 2, 1998 (see Note 5).

(3) The Association expects to eliminate its deficit during 1998. Subsequent to year end, the Association reduced the assessment for 1998 to 1% of direct premiums written and expects to receive approximately $39 million annually. The Association projects that the receipt of assessments and the continued receipt of proceeds from liquidators of insolvent insurance companies should be sufficient to satisfy the Association's obligations as they become due in 1998. 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

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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, 1997, and have issued our report thereon dated March 17, 1998. 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 maters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of the Board of Directors and management of the Louisiana Insurance Guaranty Association, the Commissioner of Insurance, State of Louisiana, and the Legislative Auditor, State of Louisiana. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Postlethwaite & Netterville

Baton Rouge, Louisiana
March 17, 1998

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