
LOUISIANA INSURANCE GUARANTY ASSOCIATION

FINANCIAL STATEMENTS
(Cash Basis)

DECEMBER 31, 2006 AND 2005

Under provisions of state law, this report is a public document. A copy of the report has been submitted to the 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.

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LOUISIANA INSURANCE GUARANTY ASSOCIATION

FINANCIAL STATEMENTS
(Cash Basis)

DECEMBER 31, 2006 AND 2005

TABLE OF CONTENTS

	<u>Page</u>
<u>Independent Auditors' Report</u>	1
<u>Financial Statements – Cash Basis</u>	
Statements of Financial Position	2
Statements of Activities	3
Notes to Financial Statements	4 – 8
<u>Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i></u>	9



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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, 2006 and 2005, 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 auditing standards generally accepted in the United States of America and 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, 2006 and 2005 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 5, 2007 on our consideration of Louisiana Insurance Guaranty Association's internal control over financial reporting and our tests of its compliance with certain provisions of laws and regulations. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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 5, 2007

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF FINANCIAL POSITION
ARISING FROM CASH TRANSACTIONS
DECEMBER 31, 2006 AND 2005

ASSETS

	<u>2006</u>	<u>2005</u>
Cash	\$ 176	\$ 1,585
Investments, at cost	<u>247,481,055</u>	<u>244,912,924</u>
	<u>\$ 247,481,231</u>	<u>\$ 244,914,509</u>

LIABILITIES AND NET ASSETS

Outstanding checks in excess of bank balances	\$ 671,125	\$ 858,180
Net assets	<u>246,810,106</u>	<u>244,056,329</u>
	<u>\$ 247,481,231</u>	<u>\$ 244,914,509</u>

The accompanying notes are an integral part of these statements.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
<u>RECEIPTS</u>		
Assessments	\$ -	\$ 10,327,986
Distributions from liquidators	9,944,363	20,668,867
Interest income	11,365,557	10,404,861
Net loss on disposition of investments	(2,021,582)	(1,975,812)
Restitution	117,063	24,455
Other income	5,833	4,183
	19,411,234	39,454,540
<u>DISBURSEMENTS</u>		
Claims paid	10,330,558	16,259,937
Unearned premiums paid	13,156	16,116
Legal fees and expenses	3,629,203	5,078,292
Claims handling costs	1,423,727	1,914,987
Return of early access distribution from liquidator	416,375	2,606,041
Professional and bank fees	360,431	365,730
Staff salaries, taxes, and benefits	237,423	225,982
Travel, meetings, and seminars	33,460	20,020
Building and renovations	16,643	37,861
Administrative expenses	196,481	313,404
	16,657,457	26,838,370
<u>EXCESS OF RECEIPTS OVER DISBURSEMENTS</u>	2,753,777	12,616,170
Net assets - beginning of the year	244,056,329	231,440,159
Net assets - end of the year	\$ 246,810,106	\$ 244,056,329

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 are required to be members of the Association (excluding the following lines of business: life, health and accident, title, disability, mortgage guaranty, and ocean marine insurance as well as all types of reinsurance).

The Association's day-to-day operations and management are performed by the Association's staff under the direction of the Board of Directors. The Association also contracts with outside staffing services, claims service providers, and other professionals to carry out these functions.

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 amounts for such liabilities.

Equipment and Facilities

The Association recognizes equipment and facilities as cash disbursements when incurred. These items are not capitalized and depreciated under the Association's cash basis of accounting.

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, 2006 and 2005:

	<u>2006</u>		<u>2005</u>	
	<u>Cost</u>	<u>Estimated Fair Value</u>	<u>Cost</u>	<u>Estimated Fair Value</u>
U.S. Government securities under agreement to sell	\$ 1,421,771	\$ 1,421,771	\$ 1,439,606	\$ 1,439,606
Money market accounts invested in U.S. Treasury obligations	1,825,754	1,825,754	638,234	638,234
U.S. Treasury notes and bonds	140,478,199	140,057,408	139,630,449	133,958,960
U.S. Government Agency obligations	<u>103,755,331</u>	<u>94,843,422</u>	<u>103,204,635</u>	<u>99,644,494</u>
	<u>\$247,481,055</u>	<u>\$238,148,355</u>	<u>\$244,912,924</u>	<u>\$ 235,681,294</u>

The Association's policy is to purchase securities issued by the U.S. Treasury and obligations issued or guaranteed by the U.S. Government and its Agencies. The estimated fair value of these securities is based on quoted market prices. The Association enters into short-term repurchase agreements with 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 accounts invested in U.S. Treasury obligations.

The Association purchases securities at premiums or discounts from the contractual maturity amount of the security. Due to the use of the cash basis of accounting, these premiums and discounts are not amortized over the holding period of the security. Instead, these differences are reported as gains or losses upon maturity or sale of the respective security. Accordingly, interest income reflects the contractual interest payments received under the investment securities.

3. Restricted Net Assets

Net assets represent funds collected from member insurance companies, distributions from liquidators, interest income, and other receipts in excess of funds disbursed to pay claims and expenses of the Association. All assets are considered 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).

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

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, 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 six 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. The Association collected no assessments from members during 2006.

5. Early Access Distributions by Liquidators

The Association files claims against the estates of insolvent insurers in an effort to recover a portion of the policyholders' claims paid and related expenses from the assets of the insolvent insurers. During the years ended December 31, 2006 and 2005, the Association received \$9,944,363 and \$20,668,867, respectively, of such distributions which are reflected as receipts in these financial statements. During the years ended December 31, 2006 and 2005, the Association also returned \$416,375 and \$2,606,041, respectively, of early access distributions previously received from liquidators under the terms of those agreements. No estimate is available of future potential distributions from liquidations due to the uncertainty and difficulty in accurately estimating these amounts.

6. Building

On December 3, 2002, the Association purchased land and a building in Baton Rouge, Louisiana to be used as a new headquarters site. The building underwent renovations and was occupied and placed into service during 2003. The cost of the building and related improvements were reflected as building expenditures during 2003 as a result of the building being put into use.

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, 2006, the Association had 2,288 open claims files outstanding, a substantial portion of which are involved in litigation. The Association is also in the process of identifying and quantifying recent insolvencies for which estimated claims liability information is considered uncertain and or incomplete. 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 estimate the amount of claims and claims administration expenses related to insolvent member insurance companies. This "reserve setting" practice is a common function of managing and administering those losses.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

NOTES TO FINANCIAL STATEMENTS

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

Provided below is an unaudited condensed balance sheet of the Association at December 31, 2006, on a modified accrual basis which recognizes management's estimate of claims and related liabilities. 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 accounting principles generally accepted in the United States of America. These estimates are expected to vary as additional information becomes available.

The condensed unaudited balance sheet below does not provide for accruals of amounts due from liquidators of insolvent insurance companies, billed but uncollected member assessments due, capitalization and depreciation of property and equipment, 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 one percent (1%) beginning January 1, 2003, which, if assessed, is estimated to produce approximately \$63 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.

ASSETS

	December 31, 2006
	<u>Unaudited</u>
Cash	\$ 176
Investments, at cost	<u>247,481,055</u>
Total assets	<u>\$ 247,481,231</u>

LIABILITIES AND NET ASSETS

Outstanding checks in excess of bank balances	\$ 671,125	
Estimated claims and claims administration expenses payable	<u>891,621,365</u>	(1)
Total liabilities	892,292,490	
Net assets (deficit)	(<u>644,811,259</u>)	(2)
Total liabilities and net assets	<u>\$ 247,481,231</u>	

(1) Represents management's estimate of claims and claims administration expense reserves related to open claim files at December 31, 2006.

The Association has been notified of 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 continues to evaluate the merits of these claims, the appropriateness of coverage under the Act, and the amount of potential liability to the Association.

LOUISIANA INSURANCE GUARANTY ASSOCIATION
BATON ROUGE, LOUISIANA

NOTES TO FINANCIAL STATEMENTS

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

Management includes in the reserve for claims and claims administration expense amounts estimated as the Association's liability for these claims based on present statutes and based on the best information available at this time. However, there are numerous and significant uncertainties regarding the amount of ultimate liability the Association may be responsible for under these claims and when amounts ultimately determined as owed by the Association become due and payable. As facts and circumstances develop, management intends to revise its estimates of these claims liabilities. Revisions in these estimates could result in significant increases or decreases in these estimates.

- (2) Due to the uncertainty of the timing and amount of claims to be paid by the Association, it is unknown whether the Association can meet its claims obligations as they become due. As described in Note 4, the Association has the statutory authority to assess up to 1% of member insureds' net direct written premiums annually if necessary to pay its obligations. The Association financial resources also include receipt of investment earnings and the continued receipt of proceeds from liquidators of insolvent insurance companies.



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**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***

Members and 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, 2006, and have issued our report there on dated March 5, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 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 reportable 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 caused by error or fraud 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.

Compliance and Other Matters

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 or other matters that are required to be reported under *Government Auditing Standards*.

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, 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

Baton Rouge, Louisiana
March 5, 2007