

AL INSURANCE

an asset is its market value or, if no
in accordance with generally accept
other generally accepted methods
of any liabilities of an insurer
accounting concepts, bases and

of any assets of the fund
which are owned by long
with value of the fund
value of the fund

The Place
555 Avenue Ave.
New York, NY
(555) 555-0000

Dear Mr. L.

I would like
to congratulate
you on your

By the way,
I would like

Thank you
for your

*Committed
to
Excellence*

**North Carolina
Insurance Guaranty Association**

2006 ANNUAL REPORT

Our Mission

is to fulfill statutorily created duties which are to provide a mechanism for the payment of covered claims as defined by the Guaranty Act, to avoid excessive delay in those payments, to avoid financial loss to claimants or policy holders because of the insolvency of an insurer, to assist in the detection and prevention of insurer insolvencies, and to provide an association to assess the cost of such protection among insurers. The manner in which our associates carry out those duties will define our excellence as an organization.

NCRB-NCRF-NCIGA



north carolina

RATE BUREAU

REINSURANCE FACILITY

INSURANCE GUARANTY ASSOCIATION



INSURANCE

North Carolina Insurance Guaranty Association

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General Organizational Information

<i>NCIGA Main Phone Number</i>	919-783-9813
<i>Facsimile</i>	919-783-5262
<i>Toll Free</i>	800-456-5086
<i>Internet Address</i>	www.ncrb.org
<i>Physical Address</i>	5401 Six Forks Road Raleigh, NC 27609

Management Contacts

Ray Evans.	Managing Secretary.	919-582-1001.	rfe@ncrb.org
R. Mike Newton.	Director, IGA	919-582-1018.	rmn@ncrb.org
Jim Auman	Director, Information Technology	919-582-1032.	jra@ncrb.org
Vicki Godbold.	Director, Human Resources	919-645-3170.	vcg@ncrb.org
David Sink.	Director, Finance & Administration	919-582-1012.	des@ncrb.org



Message from the Chairman

Mr. Allen Tomlin at the October 22, 1991 Board meeting announced that he would soon be retiring and, in the event the Board elected State Farm to serve as Chairman for the upcoming year, that Tom Huels would serve as the company's representative. The Board re-elected State Farm and I began my tenure as chairman at the Board's next meeting held November 1991. The rest is, as they say history, and this year's annual meeting will represent fifteen years that I have been privileged to serve as chairman.

At the start of my tenure, the Guaranty was involved with two large personal lines insolvencies: those being Interstate Casualty Insurance Company and American Universal Insurance Company. Then in January 1993, the Guaranty took over the obligations of handling workers' compensation claims becoming the Trustee of the existing Stock and Mutual WC Trust Accounts and responsible for the WC obligations arising from any future insolvencies.

During the remainder of the nineties there were only a few insolvencies and the Guaranty's work volume and exposure decreased. Then in October 2001, came the insolvency of Reliance Insurance Company,

still reigning as the largest insolvency ever on a state and national basis. Reliance was soon followed by PHICO, Legion, and eleven other insolvencies including two companies, Vesta Fire Insurance Corp and Shelby Insurance Company, recently liquidated in August of 2006.

Insolvencies occurring over the past five years have presented many new challenges to the Guaranty system involving complex commercial claims requiring the payment of nearly forty percent of all claim and expense payments incurred during the Guaranty's thirty years of existence.

We have met all those challenges and I wish to thank Staff, Legal Counsel, and fellow members of the Board for making it possible for the Guaranty to meet its obligation to provide a safety net for our state's insurance policyholders. I know we will continue to meet those obligations and look forward to the coming year.

Sincerely,

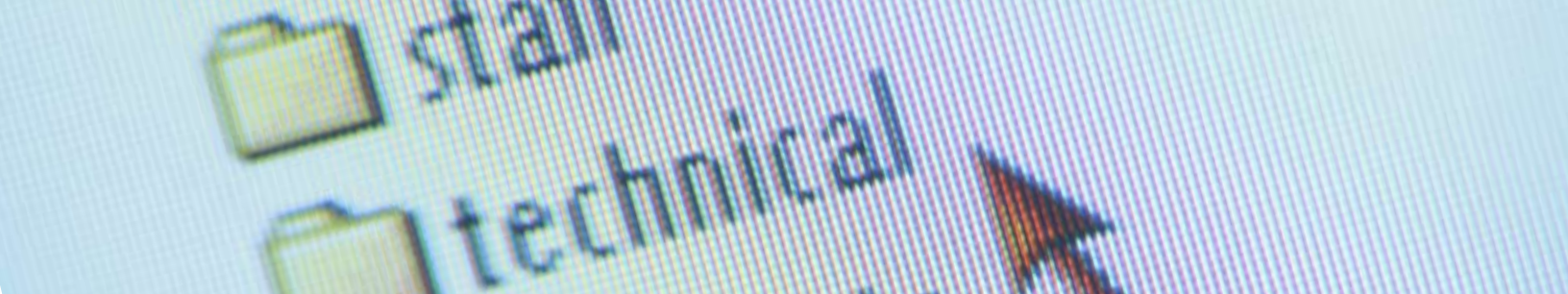
Thomas M. Huels

Chairman

“The Key to Effective Leadership is the Relationship You Build With Your Team”

Ken Blanchard Marc Muchnick





Board of Directors

The Plan of Operation provides that the Board of Directors consist of eight directors, comprised of seven elected directors, each of whom are member insurers, who shall serve three-year terms, or until their successors have been elected and qualified, and one non-voting director who shall be a property and a casualty insurance agent authorized to write insurance for a member company and who is appointed by the Commissioner of Insurance to serve for a three-year term at the pleasure of the Commissioner.

Board Member Insurers	Representative
Allstate Insurance Company	Nancy Lemke
Integon Indemnity Corporation	Art Lyon
Liberty Mutual Insurance Company	Laura Wehrle
Nationwide Mutual Insurance Company	Bob Kistner
NC Farm Bureau Mutual Insurance Company	Ron Medeiros **
State Farm Mutual Automobile Insurance Company	Tom Huels *
Travelers Indemnity Company	Benjy Seagle
NON-VOTING MEMBER	
Property & Casualty Agent	Delaine Bradsher

* Chairman (re-elected October 2005)

** Secretary- Treasurer (re-elected October 2005)

Subcommittee

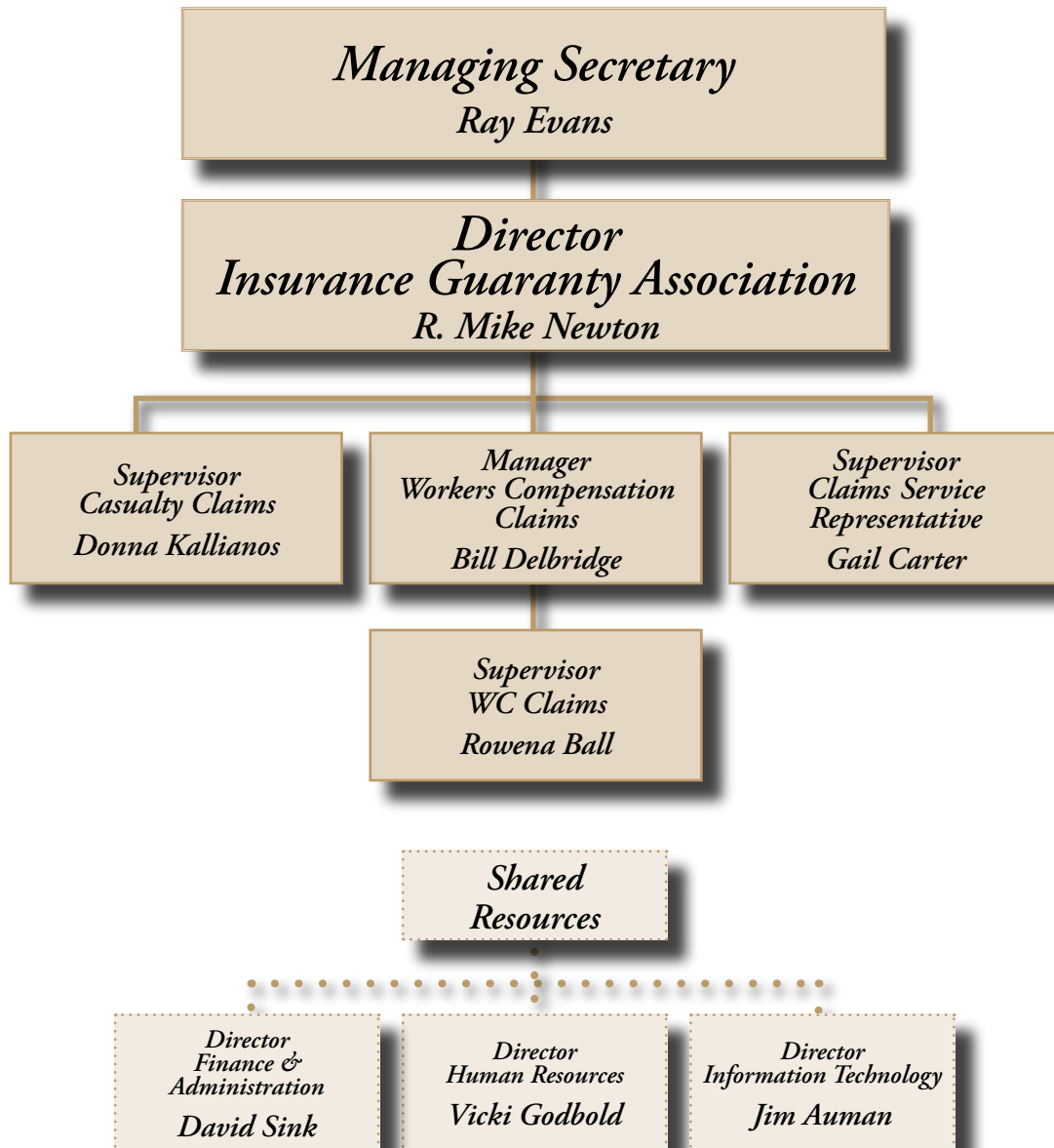
The Audit Committee oversees the financial activities of the Association and formulates recommendations for presentation to the Board of Directors.

Audit Committee Member Insurers	Representative
Nationwide Mutual Insurance Company	Bob Kistner
NCFB Mutual Insurance Company	Ron Medeiros*
Liberty Mutual Insurance Company	Laura Wehrle

* Chairman (re-elected October 2005)



NCIGA Organizational Chart





Managing Secretary's Report



With no major insolvencies and a declining number of open claims, you might think that the past year was easy. Rather than take the year off, we decided to use it to improve our operations.

Since there were fewer open claims we were able to focus on three strategies simultaneously. One was, and continues to be, a commitment to excellence in fulfilling our duties. Second was to react to fewer

claims by downsizing our operations. The third one was to work towards being better prepared for the next, inevitable round of insolvencies.

In the midst of downsizing we have maintained a focus on those strategies the Board has said are most important. These are described in detail elsewhere in this report, but I will mention several significant results of those strategies:

1. **The Guaranty Association is significantly under budget.**
2. **We have aggressively maintained the integrity of the statute resulting in many successful recoveries of paid claims.**
3. **We have completed a business continuity plan that will enable us to resume paying claims within five days of virtually any disaster.**
4. **Maybe most significant, we paid 27,000 claimant checks with virtually no complaints.**

Getting ready for the future has been centered in three areas. Most important, and now complete, is electronic storage of documents. Since the claim file from the receiver is the only record available of the history of a claim, this eliminates a serious vulnerability in the event of a disaster.

A second area is to be prepared for the financial impact of future insolvencies. We continue to maintain an arrangement with our banker for credit if needed. We currently have twenty open insolvencies and only four of those insolvencies have estimated obligations not fully funded. For those four insolvencies we have funds on hand to cover anticipated expenditures for at least two years. These amounts are detailed in the financial notes of this report.

The third area is to revisit our experiences over the past few years and evaluate the need for statutory or plan of operation changes to make future insolvencies more efficient. This is just beginning and we will have more on this soon.

None of the past year's progress would have been possible without the enthusiasm of our associates. What I have written about is change. Our folks, rather than fighting or avoiding it have embraced it.

Finally, we are grateful and pleased for the counsel, help and support of the Board, particularly the Chair Tom Huels, and committee members who have all been there when we need them.

Ray Evans, Managing Secretary





Operations Report & Analysis



In a continuing effort to improve operations, our focus in the year of “Committed to Excellence” was on three fronts: (1) continue handling claims in a fair and prompt manner; (2) seek to improve the efficiency of overall operations; and (3) ensure that we are able to continue efficient and timely operations in the event of business interruptions and future insolvencies.

During this report period the Association received 128 new claim files and closed 338 files leaving 624 files open as of August 31, 2006. The Association issued 27,245 checks during the process of paying nearly \$19.4 million in indemnity and unearned premium claims along with allocated loss expenses.

Through the efforts of Staff and Legal Counsel we continued to aggressively pursue net worth, subrogation, and large deductible recoveries utilizing the Guaranty Act’s various provisions. This year’s recoveries totaled over \$3.8 million, nearly a twenty percent recovery of funds paid out, reducing the Association’s net payout to \$15.5 million.

With the closure of some of the older estates, the maturing of the record breaking insolvencies of Reliance Insurance Company and Legion Insurance Company, and the fewest number of new claims received since fiscal year 2001, the open claim count of 624 represents the smallest number in five years. Of note is the fact that, even with the expenditure of \$15.5 million net dollars and the closure of 338 claim files, reserves on those open claims at the report year’s end exceeded the prior year’s total by \$12.7 million driven by the Workers’ Compensation (WC) book of business.

As noted, the WC book of business continued to be the focus of our claims adjustment activity as evidenced by ninety-eight percent of the indemnity and claims expense net payments (\$15.2 million) being WC in nature. Furthermore, WC claims reserves of \$70.3 million represents ninety-seven percent of total claim reserves.

Seventy-eight casualty claim files reserved at \$2.8 million remain open. These cases involve commercial exposures with most

being subject to litigation and posing interesting questions under the policy coverage and the provisions of the Guaranty Act. The \$334,000 net shown spent on indemnity and claims expense payments is skewed by nearly \$1.5 million in recoveries during the year.

Proper staffing for an operation which regularly sees volatile swings in the amount of its business presents a challenge. We continue to carefully review the number of associates in order to operate efficiently but remain mindful of our statutory duty to be able to respond to any challenge.

During this fiscal year we were able to complete the scanning of our claim files so that our “electronic” claim file is now composed of financials, adjuster reports, and supporting documents representing the entire work product. This on-line file, known as the Document Imaging Management System (DIMS), removes a weakness in our system as the physical file received from the insolvency receiver and added to during the Association’s handling of the claim often was the only copy of the file. The Association is leveraging resources with its sister organizations to develop a business continuity/ disaster recovery plan insuring our ability to provide the promised safety net to our State’s insurance buying public showing our continued commitment to excellence.

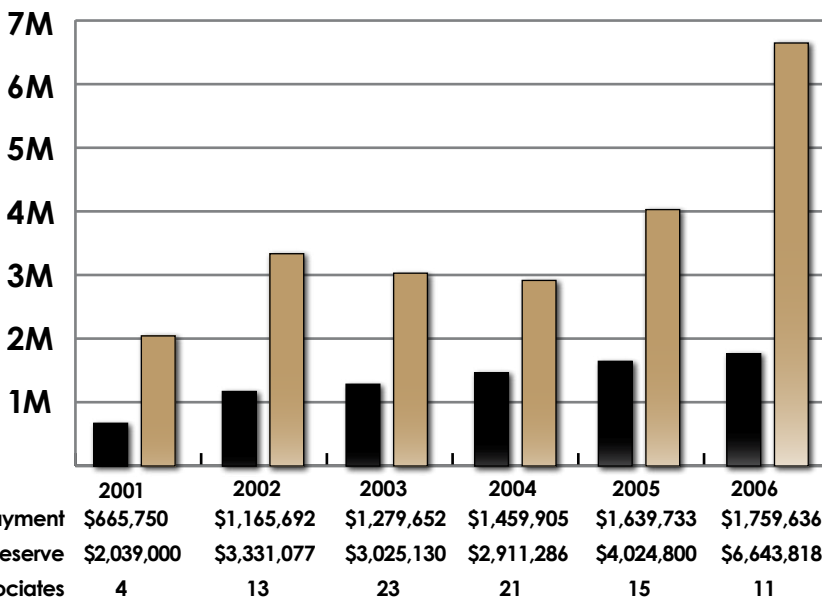
R. Mike Newton, Director, IGA



During the year 1,048 claim files involving 547,000 documents were scanned into DIMS creating electronic claim files and reducing spacing issues, allowing ease of continued work flow, and allowing a back up solution plan.

During the report period we have reduced staff from fifteen to eleven associates but feel we have retained key personnel needed to “ramp up” our operation when the next round of insolvencies develop. This graph illustrates several of the factors involved in this analysis.

 Average Payment per Associate
 Average Reserve per Associate





Report of NCIGA Counsel

In the past year, the major legal issues and outstanding litigation the Association has faced involve the following issues:

1. Statutory Reimbursements – The Association has had continuing success recovering significant reimbursements from the following sources:

A. High Net Worth Insureds

– When insureds that meet the \$50 million net worth threshold, the Association is typically able to recover the full amount it has paid on “covered claims.” A recent example is a trucking company that agreed to pay over \$336,000 as a reimbursement rather than continue a declaratory judgment action commenced by the Association. Additionally, in a case brought by the Association, Guilford Technical Community College denied its obligation as a high net worth insured to reimburse the Association on grounds of sovereign immunity. The Association prevailed over that defense at the trial court, and the case is now on appeal.

B. Large Deductibles – Where available, the Association continues to pursue reimbursements from large deductible insureds. Within the next several months, the Association anticipates receiving the following two large deductible recoveries: (1) the Association’s share of the large deductible settlement agreed to between the liquidator of Reliance Insurance Company; and (2) the Association’s share of large deductible collateral deposited with Reliance Insurance Company by Consolidated Freightways.

C. Reinsurers – As previously reported, the Association sought

reimbursement from the reinsurer for the Psychiatrists Purchasing Group program written by Legion Insurance Company. Because of the unique structure of this program, the Association contended that it had a right to be reimbursed directly by the reinsurer for “covered claims” paid by the Association. Following negotiations with the Legion liquidator and the reinsurer, the Association received a reimbursement directly from the reinsurer of over \$1.2 million.

2. Bar Dates – In the past year, the NCIGA has litigated the issue of whether claims first filed with the Association after the bar date for filing claims against the insolvent insurer constitute “covered claims.” This issue has arisen in the context of asbestos workers’ compensation claims before the North Carolina Industrial Commission. In an Opinion and Award issued on August 31, 2006, a Deputy Commissioner adopted the arguments of the Association on the bar date question. The Association anticipates that this decision will be appealed by the claimants, and may lead to activity before the General Assembly in 2007.

3. Exhaustion of Insurance of Joint Tortfeasors – In an opinion issued on February 7, 2006 in the case involving Lincoln Medical Center, the North Carolina Court of Appeals affirmed a decision in favor of the Association, and concluded that the solvent insurance coverage tortfeasor must be exhausted before recovery can be sought from the Association.

4. Insolvent Estates – In the past year, the estates of Mission Insurance Company and Mission National Insurance Company were closed in California after nearly 20 years. In the next year, the Association anticipates the closing of additional insolvent estates, which will involve submitting final amended claims with liquidators, and possible disputes over amounts to be distributed to the Association. In addition, the Association will have to make final accountings of special deposits to the North Carolina Department of Insurance in connection with these estates. Finally, in the more recent insolvencies, such as Reliance, Legion and Reciprocal of America, there may be possible disputes with liquidators over amounts to be disbursed for claims and expenses paid by the Association.

Nelson Mullins LLP



Claims Paid Detail

	WC			AUTO		
	Indemnity Paid	Expense Paid	Total Paid	Indemnity Paid	Expense Paid	Total Paid
Casualty Reciprocal	\$827,858	\$167,058	\$994,916			
Commercial Casualty				-\$30,661	\$7,605	-\$23,056
Credit General	\$206,970	\$31,605	\$238,575	\$45,000	\$6,806	\$51,806
Employers Casualty	\$34,697	\$25,433	\$60,130			
Fremont Indemnity Co	\$63,366	\$20,577	\$83,943			
Home Insurance	\$434,744	\$60,154	\$494,898			
Legion Insurance Co	\$3,139,926	\$376,547	\$3,516,473	\$550,000	\$134,259	\$684,259
LMI						
PHICO Insurance	\$296,166	\$65,261	\$361,427			
Reliance Insurance Co	\$5,286,458	\$1,072,375	\$6,358,833	-\$223,619	\$5,751	-\$217,868
ROA Insurance Co	\$567,083	\$138,310	\$705,393			
Shelby Insurance Co						
South Carolina	\$94,644	\$36,401	\$131,045	\$63,387	\$42,565	\$105,952
State Capital				\$8,500	\$4,246	\$12,746
Vesta Fire						
Villanova Insurance Co	\$1,089,864	\$166,418	\$1,256,282			
888 Mutual Trust	\$795,375	\$81,210	\$876,585			
999 Stock Trust	\$94,780	\$7,191	\$101,971			
Total	\$12,931,931	\$2,248,540	\$15,180,471	\$412,607	\$201,232	\$613,839

	ALL OTHER			TOTAL
	Indemnity Paid	Expense Paid	Total Paid	
Casualty Reciprocal				\$994,916
Commercial Casualty		\$26,755	\$26,755	\$3,699
Credit General				\$290,381
Employers Casualty				\$60,130
Fremont Indemnity Co				\$83,943
Home Insurance		\$16,518	\$16,518	\$511,416
Legion Insurance Co	-\$120,000	-\$249,212	-\$369,212	\$3,831,520
LMI				\$0
PHICO Insurance	-\$137,477	-\$43,800	-\$181,277	\$180,150
Reliance Insurance Co		\$20,660	\$20,660	\$6,161,625
ROA Insurance Co		\$1,518	\$1,518	\$706,911
Shelby Insurance Co				\$0
South Carolina	\$47,500	\$65,572	\$113,072	\$350,070
State Capital		\$20,190	\$20,190	\$32,936
Vesta Fire				\$0
Villanova Insurance Co				\$1,256,282
888 Mutual Trust				\$876,585
999 Stock Trust				\$101,971
Total	-\$209,977	-\$141,799	-\$351,776	\$15,442,535

Unearned Premium **\$95,784**

Net Total **\$15,538,319**

Recovered Net Worth and Large Deductable **\$3,547,443**

Subrogation **\$270,600**

Gross Total Expenditure **\$19,356,362**

Claims Reserve Detail

	WC				AUTO			
	Indemnity Reserve	Expense Reserve	Total Reserve	Files Pending	Indemnity Reserve	Expense Reserve	Total Reserve	Files Pending
Casualty Reciprocal	\$2,954,153	\$231,448	\$3,185,601	32				
Commercial Casualty					\$21,001	\$13,782	\$34,783	3
Credit General	\$1,721,682	\$48,302	\$1,769,984	5				
Employers Casualty	\$285,932	\$53,613	\$339,545	5				
Fremont Indemnity Co	\$1,394,986	\$153,384	\$1,548,370	4				
Home Insurance	\$2,917,987	\$272,634	\$3,190,621	41				
Legion Insurance Co	\$10,452,646	\$495,804	\$10,948,450	80	\$75,600	\$110,932	\$186,532	13
LMI	\$2	\$1	\$3	1				
PHICO Insurance	\$987,881	\$121,084	\$1,108,965	10				
Reliance Insurance Co	\$24,889,619	\$1,754,164	\$26,643,782	167	\$588,229	\$20,642	\$608,871	6
ROA Insurance Co	\$3,574,844	\$449,140	\$4,023,984	37				
Shelby Insurance Co.								
South Carolina	\$1,180,838	\$726,013	\$1,906,851	7	\$277,618	\$40,685	\$318,303	9
State Capital					\$73,000	\$12,731	\$85,731	1
Vesta Fire								
Villanova Insurance Co	\$1,644,172	\$182,135	\$1,826,307	20				
888 Mutual Trust	\$12,058,472	\$694,302	\$12,752,774	134				
999 Stock Trust	\$1,020,773	\$44,665	\$1,065,438	5				
Total	\$65,083,987	\$5,226,689	\$70,310,675	548	\$1,035,448	\$198,772	\$1,234,220	32

	ALL OTHER				TOTAL	
	Indemnity Reserve	Expense Reserve	Total Reserve	Files Pending	TOTAL RESERVES	TOTAL PENDING
Casualty Reciprocal					\$3,185,601	32
Commercial Casualty	\$19,300	\$28,175	\$47,475	8	\$82,259	11
Credit General					\$1,769,984	5
Employers Casualty					\$339,545	5
Fremont Indemnity Co					\$1,548,370	4
Home Insurance	\$37,820	\$5,823	\$43,643	7	\$3,234,265	48
Legion Insurance Co	\$101,000	\$30,365	\$131,365	3	\$11,266,347	96
LMI					\$3	1
PHICO Insurance	\$130,000	\$164,904	\$294,904	3	\$1,403,869	13
Reliance Insurance Co	\$664,442	\$66,724	\$731,166	16	\$27,983,820	189
ROA Insurance Co					\$4,023,984	37
Shelby Insurance Co.						
South Carolina	\$102,500	\$50,417	\$152,917	5	\$2,378,071	21
State Capital	\$117,400	\$18,362	\$135,762	2	\$221,493	3
Vesta Fire						
Villanova Insurance Co					\$1,826,307	20
888 Mutual Trust					\$12,752,774	134
999 Stock Trust					\$1,065,438	5
Total	\$1,172,462	\$364,770	\$1,537,232	44	\$73,082,130	624

North Carolina Insurance Guaranty Association

BALANCE SHEET

	August 31, 2005	August 31, 2006
Assets		
Cash (Checking Account)	\$852,875	\$2,010,189
Investments	60,78,136	\$76,544,332
Assessments Receivable	8,030	\$464,708
Other Assets	—	—
Total Assets	\$61,646,041	\$79,019,229
Liabilities & Fund Equity		
Accounts Payable	—	\$(59,454)
Claims Liability	\$53,345,017	\$67,291,898
Unearned Premium Liability	—	—
Claims Expense Liability	6,021,119	\$5,790,232
Outstanding Check Liability	135,093	135,093
Other Liabilities	(129)	(168)
Total Liabilities	\$60,501,100	\$73,157,600
Fund Equity	1,144,941	5,861,629
Total Liabilities & Fund Equity	\$61,646,041	\$79,019,229

INCOME STATEMENT

	Year Ending August 31, 2005	Year Ending August 31, 2006
Income		
Membership Fees	\$850	\$500
Interest Income	2,284,751	\$3,004,246
Assessments Income	6,849,774	\$22,743,086
Miscellaneous Income	16,851,219	\$11,899,139
Total Income	\$25,986,594	\$37,646,971
Expenses		
Refund To Commissioner	\$294,649	\$975,174
Refund To Member Insurers	—	1,400,000
Operating Expenses	2,638,780	2,296,040
Claims Paid (Net)	16,379,914	\$13,135,767
Claims Expenses	4,688,033	2,311,524
Premium Refunds	233,233	95,784
Total Income	\$24,234,609	\$20,214,289
Net Income	\$1,751,985	\$17,432,682

Report of Independent Auditors

The Board of Directors and Members
North Carolina Insurance Guaranty Association

We have audited the accompanying statements of cash receipts and disbursements of the North Carolina Insurance Guaranty Association (the Association) for the years ended December 31, 2005 and 2004. 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1, the statements of cash receipts and disbursements present a summary of cash activity and are not intended to be a presentation in conformity with accounting principles generally accepted in the United States.

In our opinion, the statements referred to above present fairly, in all material respects, the cash receipts and disbursements of the North Carolina Insurance Guaranty Association for the years ended December 31, 2005 and 2004, and its cash and investment balances at December 31, 2005 and 2004.

Ernst & Young LLP

April 18, 2006

Shared Resources



Jim Auman

Director, Information Technology



Vicki Godbold


Director, Human Resources



David Sink

Director, Finance &
Administration

NORTH CAROLINA RATE BUREAU
NORTH CAROLINA REINSURANCE FACILITY
NC INSURANCE GUARANTY ASSOCIATION



North Carolina
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