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# REPORT OF THE ANNUAL MEETING

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April 24, 2007

Insurance Placement Facility of Pennsylvania

530 Walnut Street, Suite 1650  
Philadelphia, PA 19106-3698

Board of Directors

2006 - 2007

Ms. Joanne K. Martyn, Chairperson . . . . .	Chubb Group of Insurance Companies
Mr. John D. Fillippo . . . . .	ACE USA
Ms. Susan A. Erney . . . . .	The Harleysville Insurance Companies
Mr. William W. Martin . . . . .	The Hartford
Mr. Terry McConnell . . . . .	Erie Insurance Group
Ms. Andrea Short . . . . .	Allstate Insurance Companies
Ms. Marci Thomas . . . . .	State Farm Insurance Companies
Mr. Daniel M. Taylor, Jr., Esq., General Counsel . . . . .	Swartz Campbell, LLC
Mr. John M. Ogle, General Manager . . . . .	Insurance Placement Facility of Pennsylvania

AGENDA FOR THE ANNUAL MEETING

INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA

April 24, 2007 - 1:30 P.M.

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1. Call to Order - 1:30 P.M. - Ms. Joanne K. Martyn, Chairman, presiding
2. Approval of Minutes of Previous Year Annual Meeting - April 27, 2006
3. Ratification of Board Action
4. Report of the Chairman
5. Report of the General Manager
6. Treasurer's Report
7. Other Business
8. Election of Board of Directors 2007 - 2008

Nominations are :

- 1) ACE USA
  - 2) Allstate Insurance Company
  - 3) Chubb Group of Insurance Companies
  - 4) Erie Insurance Group
  - 5) State Farm Insurance Companies
  - 6) The Harleysville Insurance Companies
  - 7) The Hartford
9. Adjournment of Meeting

Insurance Placement Facility of Pennsylvania  
Minutes of the Annual Meeting  
April 24, 2007  
Administrative Offices of the Facility  
1:30 p.m.  
530 Walnut Street, Suite 1650  
Philadelphia, PA

The Annual Meeting of the Insurance Placement Facility of Pennsylvania was called to order with Chairperson Ms. Joanne K. Martyn presiding. General Manager John M. Ogle served as secretary and reported that a quorum was present in person or by proxy. Mr. Ogle reported that attendees represented 172 companies or 76.53 % of the membership.

Upon motion duly made, seconded and carried, the Minutes of the April 27, 2006 Annual Meeting were approved as distributed.

A motion to ratify the actions of the Board of Directors for the 2006-2007 term was duly made, seconded and carried.

Motions were made, seconded and carried to waive the reading of the Chairman's report, the General Manager's report and the Treasurer's report as all three reports will be incorporated into the Annual Report submitted to Member Companies. The reports were accepted as presented.

The General Manager noted the 2006 financial audit report provided by the accounting firm of Smart and Associates, LLP as presented to the Board of Directors will be made part of the Annual Report submitted to Member Companies.

With no other new business, Nominating Committee Chairman Mr. William W. Martin, placed into nomination the following Member Companies to serve on the Board of Directors for the 2007-2008 term.

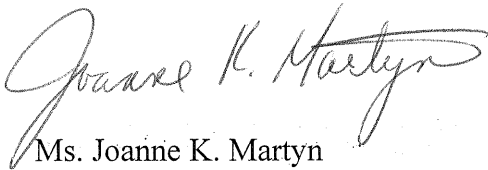
ACE USA  
Allstate Insurance Companies  
Chubb Group of Insurance Companies  
Erie Insurance Group  
State Farm Insurance Companies  
The Harleysville Insurance Companies  
The Hartford

There being no other nominations, it was moved, seconded and carried to close nominations. Chairperson Martyn requested and received confirmation from the secretary that a sufficient amount of ballots had been cast for the nominees. Mr. Ogle reported that 163 companies representing 75.89 % of the membership indicated their intention to cast ballots in person or by proxy in favor of the nominees. Therefore, upon motion duly made seconded and carried, the slate was declared elected.

The next annual meeting was set for April 2008.

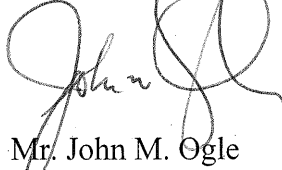
There being no further business and upon motion duly made, seconded and carried, the meeting was adjourned.

Approved by



Ms. Joanne K. Martyn  
Chairperson of the Board

Respectfully submitted by,



Mr. John M. Ogle  
General Manager

Report of the Chairman  
Ms. Joanne K. Martyn

39<sup>th</sup> Annual Meeting  
of the Members of  
Insurance Placement Facility of Pennsylvania  
April 24, 2007

Good Afternoon and welcome to the 39<sup>th</sup> Annual Meeting of the members of the Insurance Placement Facility of Pennsylvania. As Chairman, it is my pleasure to report on the operations of the association for the past year. Although the General Manager will cover some of the details in his report, I am very pleased to report to you that the association continues to fully meet its obligations as required by the relevant Pennsylvania statutes and regulations.

From a business perspective, the Pennsylvania marketplace appears to be extremely healthy and competitive. As such, the association saw its business continue to decline. In 2006, the Pennsylvania FAIR Plan recorded \$13,605,581 in Earned Premium. Losses Incurred totaled \$6,148,865 and Loss Adjustment Expense Incurred totaled \$1,018,280. Underwriting Expenses totaled \$4,786,468 resulting in a year end Underwriting Surplus of \$1,651,968. Taking into account Investment Income and Other Income and Expenses, the Pennsylvania FAIR Plan finished 2006 with a surplus of \$2,157,264.

Over the past four decades the Pennsylvania FAIR Plan has issued more than 2,600,000 policies and wrote over \$450 million in premium. During that time, the Plan experienced many times of rapid growth as well as double digit percentage declines. The current depopulation trend, which began in late 2004 and is expected to continue into 2007, is another challenge in the long history of the Plan. Regardless of the amount of business activity, the Plan stands ready to meet its obligations to provide high quality service to its customers.

As we have done for more than 38 years, the Pennsylvania FAIR Plan has provided management and functional support to the Insurance Placement Facility of Delaware. In 1986, the Pennsylvania Plan also began to provide that same service to the West Virginia Essential Property Insurance Association. Although both of these operations are considerably smaller than the Pennsylvania Plan, the Plan management operates each Plan with the same high quality and professional services that are expected.

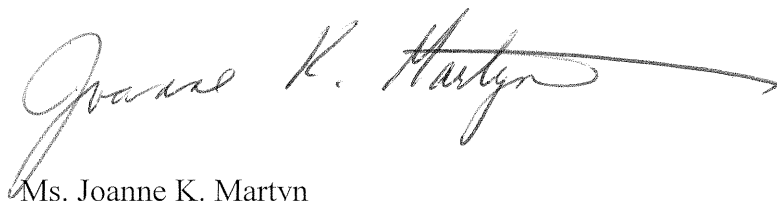
As I step down as Chairman, I would like to thank General Manager John Ogle and his management staff for all of their efforts. At the same time, I would like to recognize each of the employees for their continuing efforts to provide service in a timely and efficient manner to the policyholders, agents and brokers as well as the various member companies and regulatory personnel.

I would also be remiss if I did not recognize the fine efforts and leadership of the Pennsylvania Insurance Department. In particular, I would like to thank Pennsylvania Insurance Commissioner Diane Koken for all her assistance to the operation.

As I step away from my role as Chairman, I would also like to thank General Counsel Dan Taylor for his tireless service to the organization. Dan has provided the Board with his review and advice on a variety of issues. His opinions have served the Plan and the Board well. In addition, I would like to thank our Committee Chairmen and in particular Claim Committee Chairman, Bob Barber, Underwriting Chairman, Terry McConnell and Accounting Committee Chairman Tom Sykes for having assisted the Plan Manager and the Board in overseeing the operation.

Lastly, this past year has brought many new faces to our Board of Directors and its committees. To those individuals who have left our organization I would like to express my best wishes for their future endeavors and my gratitude for their past contributions. I would like to thank my fellow Board Members for their participation and support. The job of Chairman carries its own demands, but the job performed by my fellow board members and Committee Members has certainly made my job as Chairman much easier.

Respectfully submitted,

A handwritten signature in cursive script that reads "Joanne K. Martyn". The signature is written in black ink and has a long, sweeping horizontal line extending to the right from the end of the name.

Ms. Joanne K. Martyn  
Chairman of the Board

Report of the General Manager  
John M. Ogle  
Annual Meeting of the Insurance Placement Facility of Pennsylvania  
April 24, 2007  
Philadelphia, Pennsylvania  
1:30 p.m.

Good Afternoon and welcome to the 39<sup>th</sup> annual meeting of the Insurance Placement Facility of Pennsylvania. Nationally, the year 2006 was a time of re-evaluation in the insurance industry and the future promises to bring new challenges. In Pennsylvania; however, the marketplace appears to have remained healthy and competitive. The weather has been favorable and generally speaking, the year was successful. I am pleased to report in 2006, the Insurance Placement Facility of Pennsylvania continued to meet the purposes of the Plan by providing and servicing a basic property insurance policy to the citizens of Pennsylvania.

In preparation for this meeting I looked back at the minutes and notes from the early meetings of the Insurance Placement Facility of Pennsylvania. Many of those discussions in the late 1960's were filled with uncertainty and doubt for the future. Those individuals worked under the cloud of social unrest in the urban cities, and were unconcerned with today's prospect of terrorism or a mega-catastrophe. I also noted that the participants in those meetings, all familiar names, were people no longer working within the insurance industry. Each year as they retire, we lose their perspective, expertise and their first hand knowledge. It remains; however, our responsibility to ensure that the FAIR Plan continues to meet not only the purposes of the Plan as envisioned in 1968 but also as it applies to 2007 and beyond.

Since 1968, the Pennsylvania FAIR Plan has issued just under 2,603,000 policies and collected more the \$447,790,000 in premiums while incurring slightly less than \$304,800,000 in losses. As for 2006, our 38<sup>th</sup> full year of operation, the FAIR Plan issued just 40,204 policies which is a decline of nearly 9% from 2005. The declining policy counts are a continuation of a depopulation trend originally established in 2004. On the claims side, the FAIR Plan experienced a decline in claim counts, but an increase in severity. Loss payments rose 33% to \$6,753,386 and the average payment increased nearly 32.5% to \$10,946 per claim. Despite the declining volume and increased claim payments, the Facility recorded a year end 2006 Underwriting Surplus of \$1,651,968 which continues a string of surplus quarters dating back several years.

This past year was uneventful for the Pennsylvania FAIR Plan as we incurred few weather

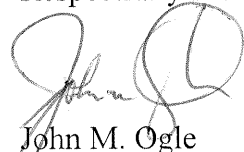


This past year was uneventful for the Pennsylvania FAIR Plan as we incurred few weather related losses nor were we involved in any major litigation. Despite a continuation of less new business and less policies issued, staff was very busy preparing for the future. In 2006, staff revised our website to be far more interactive, including adding a feature to allow for the electronic completion, submission and payment of new applications. Staff also revised our procedures, updated our disaster recovery process, installed a new computer system and eliminated forms, filing areas and rental spaces.

None of this would have been possible without the dedication and tireless efforts of my very fine staff. Each department faces considerable challenges throughout the year and I think the individual contributions of the employees should be recognized. Each employee at the Plan performs functions that impact or places demands on their fellow employees. That process can be routine or complex. It can be smoothly executed or be an exercise in frustration, but in all cases, I am impressed with the Staff's professionalism and attention to detail. I would like to take this opportunity to thank each member of the Staff for their contributions

I would be remiss if I did not note the efforts of each member of the Board of Directors and the members of our various Committees. Each of those individuals so freely gives us their expertise and wisdom for the betterment of the organization. I would also like to personally thank our outgoing Chairperson Joanne Martyn, for her dedicated service to this organization. I'm quite sure much of the success of the organization was a result of her leadership and abilities. I would also like to thank General Counsel, Daniel Taylor, of the law firm of Swartz Campbell. Dan provided us with well thought out legal advice and I am grateful for his contributions. In closing I would also like to thank the staff of the Pennsylvania Insurance Department and in particular, Commissioner Diane Koken. Because of the efforts of all, I feel confident the organization is ready for whatever the future may bring and I look forward to the challenges of the coming years.

Respectfully submitted,



John M. Ogle  
General Manager

# INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA

## PENNSYLVANIA FAIR PLAN

### Treasurer's Report

December 31, 2006

#### ASSETS

Cash in Bank	2,212,755.77
Investments, Short term at cost plus accumulated discount	11,828,876.90
Accrued Investment Income	0.00
Due from Participating Members	0.00
Premiums Receivable	12,239.40
Other Receivables	236,967.42
Prepaid Premium Tax	0.00
Equipment *	0.00
Total Assets	<u>14,290,839.49</u>

#### LIABILITIES AND MEMBERS' EQUITY

Unearned Premiums	6,514,591.00
Unearned Advance Premiums	321,562.00
Outstanding Losses	1,779,223.00
Outstanding Loss Adjustment Expenses	292,100.00
Accrued Expenses	102,650.00
Unpaid Post Retirement Benefits	1,031,520.00
Unpaid Pension	645,235.00
Accounts Payable	177,578.25
Claims Checks Payable	903,504.10
Unpaid Premium Tax	4,749.86
Total Liabilities	<u>11,772,713.21</u>
Members' Equity (Deficit)	<u>2,518,126.28</u>
Total Liabilities and Members' Equity	<u>14,290,839.49</u>

Respectfully Submitted,



RoseMarie McDonald  
Accounting Manager

\* E. D. P. Equipment

**INSURANCE PLACEMENT FACILITY  
OF PENNSYLVANIA**

Statutory Financial Statements,  
Independent Auditors' Report and  
Supplemental Schedules

For the years ended December 31, 2006 and 2005

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**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
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For the years ended December 31, 2006 and 2005

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## Independent Auditors' Report

The Board of Directors  
Insurance Placement Facility of Pennsylvania

We have audited the accompanying statutory statements of admitted assets, liabilities, and members' equity (deficit) of Insurance Placement Facility of Pennsylvania (the "Facility") as of December 31, 2006 and 2005, and the related statutory statements of operations and members' equity (deficit) and cash flows for the years then ended. These statutory financial statements are the responsibility of the Facility's management. Our responsibility is to express an opinion on these statutory financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit 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 more fully in Note 1 to the statutory financial statements, the Facility prepared these statutory financial statements using accounting practices prescribed or permitted by the Insurance Department of the Commonwealth of Pennsylvania, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

The Facility's liabilities exceeded its assets by \$205,069 at December 31, 2005. Such amounts, however, are recoverable from member companies (Note 2).

In our opinion, the statutory financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and members' equity (deficit) of Insurance Placement Facility of Pennsylvania as of December 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in Note 1.

Our audits were made for the purpose of forming an opinion on the statutory-basis financial statements taken as a whole. The accompanying supplemental investment disclosures, as of and for the year ended December 31, 2006, are presented to comply with the National Association of Insurance Commissioner's Accounting Practices and Procedures manual and is not a required part of the statutory-basis financial statements. Such information has been subjected to the auditing procedures applied in our audit of the statutory-basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory-basis financial statements taken as a whole.

This report is intended solely for the information and use of the Facility and for filing with the Insurance Department of the Commonwealth of Pennsylvania and other state insurance departments to whose jurisdiction the Facility is subject and is not intended to be and should not be used by anyone other than these specified parties.

*Smart and Associates, LLP*

April 12, 2007

SMART and Associates, LLP  
Certified Public Accountants  
80 Lancaster Avenue | Devon, PA 19333 | 610.254.0700 | Fax 610.254.5293 | [www.smartgrp.com](http://www.smartgrp.com)

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**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Statutory Statements of Admitted Assets, Liabilities and Members' Equity (Deficit)  
December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
<b>ADMITTED ASSETS</b>		
Fixed maturities at amortized cost	9,940,008	9,510,544
Cash and cash equivalents	4,101,625	3,863,253
Due from related parties	236,967	132,821
Premiums receivable	<u>12,239</u>	<u>30,594</u>
 Total admitted assets	 <u><u>\$ 14,290,839</u></u>	 <u><u>\$ 13,537,212</u></u>
<b>LIABILITIES AND MEMBERS' EQUITY (DEFICIT)</b>		
Liabilities:		
Unearned premiums	6,514,591	7,068,779
Claims/drafts payable	903,504	673,480
Unpaid losses and loss adjustment expenses	2,071,323	3,026,055
Unearned advanced premiums	321,562	327,203
Postretirement benefits payable	1,031,520	1,114,548
Pension liability	645,235	1,257,407
Other liabilities	<u>284,977</u>	<u>274,809</u>
 Total liabilities	 11,772,712	 13,742,281
 Members' equity (deficit)	 <u>2,518,127</u>	 <u>(205,069)</u>
 Total liabilities and members' equity (deficit)	 <u><u>\$ 14,290,839</u></u>	 <u><u>\$ 13,537,212</u></u>

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

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Statutory Statements of Operations and Members' Equity (Deficit)  
For the years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Underwriting:		
Premiums earned	13,605,581	13,705,654
Less:		
Losses incurred	6,148,865	5,073,731
Loss adjustment expenses incurred	1,018,280	1,482,850
Underwriting and other expenses incurred	4,635,423	4,681,749
	<u>11,802,568</u>	<u>11,238,330</u>
Net underwriting gain	<u>1,803,013</u>	<u>2,467,324</u>
Investment income	<u>510,596</u>	<u>232,815</u>
Other income (expense):		
Premiums receivable charged off	(9,961)	(11,343)
Other income	4,662	37,175
	<u>(5,299)</u>	<u>25,832</u>
Other (expense) income, net	<u>(5,299)</u>	<u>25,832</u>
Net income	2,308,310	2,725,971
Members' deficit, beginning of year	(205,069)	(2,507,910)
Change in nonadmitted assets	(50,036)	34,308
Change in additional minimum pension liability	461,126	(457,438)
Refunds/assessments charged-off	3,796	-
Members' equity (deficit), end of year	<u>\$ 2,518,127</u>	<u>\$ (205,069)</u>

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

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Statutory Statements of Cash Flows  
For the years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities:		
Premiums collected, net	\$ 13,075,856	\$ 13,747,929
Loss and adjustment expenses paid (net of salvage and subrogation)	(8,121,877)	(6,351,594)
Underwriting expenses paid	(5,256,738)	(4,890,367)
Investment income	510,596	167,677
Premiums receivable charged off	(9,961)	(11,343)
Other income	5,431	37,175
	<u>203,307</u>	<u>2,699,477</u>
Cash flows from investing activities:		
Proceeds from investments sold, matured, or repaid:		
Fixed maturity investments	20,617,000	17,164,000
Cost of investments acquired:		
Fixed maturity investments	<u>(20,619,431)</u>	<u>(19,663,082)</u>
	<u>(2,431)</u>	<u>(2,499,082)</u>
Cash flows from financing and other miscellaneous activities:		
Refunds/assessments charged-off	3,796	-
Other, net	33,700	93,919
	<u>37,496</u>	<u>93,919</u>
Net increase in cash and cash equivalents	238,372	294,314
Cash and cash equivalents, beginning of year	<u>3,863,253</u>	<u>3,568,939</u>
Cash and cash equivalents, end of year	<u>\$ 4,101,625</u>	<u>\$ 3,863,253</u>

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



## INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA

Notes to Statutory Financial Statements  
For the years ended December 31, 2006

### I. Summary of Significant Accounting Policies:

The statutory financial statements of Insurance Placement Facility of Pennsylvania (the "Facility") have been prepared on the basis of accounting practices prescribed or permitted by the National Association of Insurance Commissioners ("NAIC") and the Insurance Department of the Commonwealth of Pennsylvania.

The more significant accounting policies are as follows:

#### Premiums:

Premiums are recognized as revenues ratably over the terms of the policies. Unearned premiums are computed on the monthly pro rata basis.

#### Commissions:

Commissions and other costs of acquiring business are charged to operations as incurred.

#### Nonadmitted Assets:

Certain assets designated as "nonadmitted" are not reflected in the statutory statements of admitted assets, liabilities, and members' equity (deficit). Nonadmitted assets include furniture, fixtures, and leasehold improvements and are charged directly against members' equity (deficit).

#### Unpaid Losses and Loss Adjustment Expenses:

Unpaid losses and loss adjustment expenses are estimated based on losses reported and the Facility's past experience for losses incurred but not yet reported. Management believes that such provisions are adequate to cover the ultimate liability. However, such estimates could differ from the amounts ultimately paid when claims are settled. Subsequent changes in estimates are reflected in earnings currently.

#### Use of Estimates:

The preparation of statutory financial statements in conformity with statutory accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the statutory financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### Invested Assets:

Bonds are carried at values prescribed by the Securities Valuation Office ("SVO") of the NAIC. Bonds are generally carried at amortized cost. Estimated fair value of bonds is determined using values prescribed by the SVO that approximate quoted market values. Charges associated with investments that are other than temporarily impaired are reflected within the statutory statements of operations. Realized investment gains or losses are determined using the specific-identification method.

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Notes to Statutory Financial Statements, continued  
For the years ended December 31, 2006

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1. Summary of Significant Accounting Policies, continued:

Cash and Cash Equivalents:

Cash and cash equivalents include cash on hand and other highly liquid temporary investments. The carrying value of cash equivalents approximates fair value. Interest and dividend income from cash and cash equivalents is included in investment income on the statutory statements of operations.

Variances from Generally Accepted Accounting Principles:

Certain of the prescribed or permitted insurance accounting practices followed by the Facility differ from accounting principles generally accepted in the United States of America. The principal differences are as follows:

- Commissions and other acquisition costs, if recoverable from future operations, would be deferred and charged against operations on the same basis that related premiums are recognized as revenues.
- Certain assets designated as “nonadmitted” would be reflected in the statutory statements of admitted assets, liabilities, and members’ equity (deficit).
- Fixed income securities are carried at amortized cost regardless of their classification.
- Calculation of the pension obligation excludes non-vested employees.

The effects on the statutory financial statements of these differences have not been determined.

Reclassifications:

Certain prior year amounts have been reclassified to conform to the current year presentation.

2. General:

The Facility was created by an act of the General Assembly of the Commonwealth of Pennsylvania (The Pennsylvania Fair Plan Act) to make available basic property insurance against fire and other perils for residential and business properties located in the Commonwealth. Each authorized insurance company in the Commonwealth participates in the profits and losses of the Facility in the proportion that certain premiums written in the Commonwealth by each company during the second preceding calendar year bear to the aggregate of such premiums written by all authorized companies and is subject to future cash assessments, if required. The Members’ deficit of \$205,069 at December 31, 2005, may ultimately be assessed to the participating companies.

The Facility shares office space and the service of certain employees with the Insurance Placement Facility of Delaware and the West Virginia Essential Property Insurance Association, both of which pay the Facility a portion of such joint expenses based on estimates of actual usage.

3. Federal Income Taxes:

The Facility files as a partnership for federal income tax purposes. Consequently, the Facility provides each member company with an annual statement of its relative share of the Facility’s annual results of operations for inclusion in each participating member’s tax return.

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

4. Investments:

Investments as of December 31, 2006, the amortized cost and NAIC market value of investments in fixed maturities are as follows. NAIC market value approximates estimated fair value.

<u>2006</u>	<u>Amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>NAIC market value</u>
U.S. Treasury securities and obligations of U.S. government corporations and agencies	\$9,940,008	\$ -	\$ 53,094	\$9,886,914
<u>2005</u>	<u>Amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>NAIC market value</u>
U.S. Treasury securities and obligations of U.S. government corporations and agencies	\$9,510,544	\$ -	\$ 14,699	\$9,495,845

All fixed maturity investments at December 31, 2006, have contractual maturity dates within one year.

Proceeds from the sales of fixed maturities during the year ended December 31, 2006 were \$20,617,000. Gross gains of \$409,343 were realized on those sales during 2006.

The components of net investment income earned for the years ended December 31, 2006 and 2005 are as follows:

	<u>2006</u>	<u>2005</u>
Fixed maturities	\$ 427,034	\$ 185,554
Cash and short-term investments	83,562	47,261
Investment income	<u>\$ 510,596</u>	<u>\$ 232,815</u>

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

5. Employee Benefits:

The Facility, in conjunction with the Insurance Placement Facility of Delaware and the West Virginia Essential Property Insurance Association and other unaffiliated organizations, is a participant in the Prudential Retirement Insurance and Annuity Company Pension Plan, which covers all of its employees. The pension plan qualifies under the provisions of Section 501(a) of the Internal Revenue Code and is exempt from federal income taxes. The pension plan is funded through the trustee by contributions to group annuity contracts with two insurance companies.

The Facility uses a December 31 measurement date for its pension plan. Assets, liabilities and expenses of the plan are allocated to the Facility based on its underwriting activity. The allocation percentage used for the Facility was 89.59% in 2006 and 90.31% in 2005.

The following table sets forth the year-end status of the plan:

	<u>2006</u>	<u>2005</u>
Change in projected benefit obligation:		
Benefit obligation at January 1	\$ 8,968,928	\$ 7,732,694
Service cost	197,895	202,812
Interest cost	493,638	465,463
Actuarial (gain) loss	(397,430)	794,494
Benefits paid	<u>(238,989)</u>	<u>(226,535)</u>
Benefit obligation at December 31	<u>9,024,042</u>	<u>8,968,928</u>
Change in plan assets:		
Fair value of plan assets at January 1	6,306,500	5,735,967
Actual return on plan assets	473,103	448,035
Employer contributions	510,119	349,033
Benefits paid	<u>(238,989)</u>	<u>(226,535)</u>
Fair value of plan assets at December 31	<u>7,050,733</u>	<u>6,306,500</u>
Funded status	(1,973,309)	(2,662,428)
Unrecognized net actuarial loss	<u>1,608,223</u>	<u>2,144,390</u>
	<u>\$ (365,086)</u>	<u>\$ (518,038)</u>

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Notes to Statutory Financial Statements, continued  
For the years ended December 31, 2006

5. Employee Benefits, continued:

Weighted average assumptions used to determine benefit obligations at December 31:

	<u>2006</u>	<u>2005</u>
Discount rate	6.00%	5.50%
Rate of compensation increase	3.50%	3.25%

The net periodic pension cost for the plan includes the following components:

	<u>2006</u>	<u>2005</u>
Components of net periodic pension cost:		
Service cost	\$ 197,895	\$ 202,812
Interest cost	493,638	465,463
Expected return on plan assets	(503,639)	(492,289)
Amount of loss recognized	<u>169,273</u>	<u>117,588</u>
Net periodic pension cost	<u>\$ 357,167</u>	<u>\$ 293,574</u>

Weighted average assumptions used to determine the net periodic pension cost:

	<u>2006</u>	<u>2005</u>
Discount rate	6.00%	5.50%
Expected long-term rate of return	8.00%	8.50%
Weighted average rate of compensation increase	3.25%	3.25%

The accumulated benefit obligation for the plan was \$7,770,941 and \$7,694,367 at December 31, 2006 and 2005, respectively.

Accrued benefit cost was \$720,208 and \$1,387,867 at December 31, 2006 and 2005, respectively.

An additional minimum pension liability ("AML") is required when the actuarial present value of the accumulated plan benefit obligation exceeds plan assets and accrued pension liabilities. As of December 31, 2006 and 2005, the plan's had an AML of \$355,122 and \$869,829, respectively. Pursuant to the requirements of SSAP No. 89, changes to the AML are recorded directly to members' equity (deficit). The increase (decrease) in the AML during 2006 and 2005, respectively was (\$514,707) and \$560,358.

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

5. Employee Benefits, continued:

The benefit obligation excludes liabilities for nonvested employees, which were \$11,355 and \$6,899 at December 31, 2006 and 2005, respectively.

The expected long-term rate of return on assets assumption is 8.00%. As defined in Financial Accounting Standards ("FAS 87"), this assumption represents the rate of return on plan assets reflecting the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the benefit obligation. The assumption has been determined by reflecting expectations regarding future rates of return for the investment portfolio, with consideration given to the distribution of investments by asset class and historical rates of return for each individual asset class.

The plan's weighted average asset allocations at December 31, 2006 and 2005, by asset category are as follows:

	2006	2005
Asset category:		
Equity securities	61.7%	59.6%
Debt securities	36.4%	39.7%
Cash	1.9%	0.7%

The primary investment objective for the pension plan assets is to achieve maximum rates of return commensurate with safety of principal, given the asset mix, credit quality and diversification guidelines and restrictions approved by the plan administrator's board of directors. The pension asset allocation is reviewed quarterly to determine whether the portfolio mix is within an acceptable range of target allocation. Target asset allocations are based on asset and liability studies with the goal to enhance the expected return of the pension portfolio while maintaining acceptable levels of risk. The target asset allocation is 60% equity securities and 40% debt securities.

Contributions to the plan are expected to be \$569,838 in 2007.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2007	\$ 286,000
2008	332,000
2009	351,000
2010	377,000
2011	448,000
2012-2016	3,077,800

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

5. Employee Benefits, continued:

The Facility provides life insurance for active employees upon the date of hire. The amount of insurance provided is equal to two times the employee's basic annual salary. For employees who are under age 65 at retirement, the Facility continues to pay the full cost of life insurance until the employee reaches age 65, at which time coverage is reduced to \$5,000. For employees who retire at age 65 or older, the Facility pays the full cost of life insurance with coverage limited to \$5,000.

Retired employees of the Facility are provided Medicare HMO coverage. The HMO provides coverage for certain hospital, surgical, and medical costs not covered by Medicare. To be eligible for the HMO, a retiree must be 65 years of age or older and have at least five years of service with the Facility.

The Facility uses a December 31 measurement date for its postretirement benefit plan.

The following table sets forth the postretirement health care and life insurance benefit plan's funded status as of December 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Accumulated postretirement benefit obligation:		
Postretirement benefit obligation for retirees and fully vested plan participants	\$ 446,038	\$ 470,580
Accumulated postretirement benefit obligation in excess of plan assets	446,038	470,580
Unrecognized gain	538,968	560,987
Unrecognized prior service	<u>166,372</u>	<u>198,619</u>
Accrued postretirement benefit cost	<u>\$ 1,151,378</u>	<u>\$ 1,230,186</u>

The following table represents a reconciliation of postretirement benefit cost for the years ended December 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Accrued postretirement benefit cost at January 1	\$ 1,230,186	\$ 1,355,385
Benefit income for year	(47,650)	(47,381)
Benefits paid during year	<u>(31,158)</u>	<u>(77,818)</u>
Accrued postretirement benefit cost at December 31	<u>\$ 1,151,378</u>	<u>\$ 1,230,186</u>

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

5. Employee Benefits, continued:

Weighted average assumptions used to determine benefit obligations at December 31:

	<u>2006</u>	<u>2005</u>
Discount rate	6.00%	5.50%
Rate of compensation increase	3.50%	3.25%

Net periodic postretirement benefit cost for 2006 and 2005 includes the following components:

	<u>2006</u>	<u>2005</u>
Service cost/eligibility cost	\$ -	\$ -
Interest cost	25,189	27,148
Amortization of gain	(32,247)	(32,247)
Amortization of prior service cost	<u>(40,592)</u>	<u>(42,282)</u>
Net periodic postretirement benefit cost	<u>\$ (47,650)</u>	<u>\$ (47,381)</u>

Weighted average assumptions used to determine the net periodic postretirement cost:

	<u>2006</u>	<u>2005</u>
Discount rate	5.50%	5.75%
Weighted average rate of compensation increase	3.25%	3.50%

For measurement purposes, for participants younger than age 65, healthcare cost trend increases of 10% and 11% were assumed for 2006 and 2005, respectively. These rate increases were assumed to decrease through 2011 and later when they level off at 5%. The healthcare cost trend rate assumption has an effect on the amounts reported. For example, increasing the assumed healthcare cost trend rate by one percentage point in each year would increase the accumulated postretirement benefit obligation as of December 31, 2006 by \$42,758 and net periodic postretirement benefit cost for the year ended December 31, 2006 by \$2,409.



**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Notes to Statutory Financial Statements, continued  
For the years ended December 31, 2006

5. Employee Benefits, continued:

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2007	\$ 32,735
2008	37,162
2009	39,526
2010	39,522
2011	42,375
2012-2016	273,916

The employees of the Facility are eligible to participate in the Benefits Connection Group 401(k) Savings Plan, a defined contribution plan. The plan is administered by the Administration Committee for Benefits Connection Group Savings Plan. Participation in the plan is voluntary. Employees are vested in employer contributions upon participation. Employees may contribute 1% to 16% of their annual compensation on a before-tax basis and/or 1% to 16% of their annual compensation on an after-tax basis for a total of 16%. The Facility matches employee contributions up to a maximum of 6% of an employee's annual compensation. Contributions by the Facility amounted to \$102,426 and \$98,059 in 2006 and 2005, respectively.

6. Liability for Unpaid Losses and Loss Adjustment Expenses:

Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows:

	<u>2006</u>	<u>2005</u>
Balance, January 1	<u>\$ 3,026,055</u>	<u>\$ 2,821,068</u>
Incurred related to:		
Current year	7,958,189	6,776,070
Prior years	<u>(791,044)</u>	<u>(219,489)</u>
Total incurred	<u>7,167,145</u>	<u>6,556,581</u>
Paid related to:		
Current year	6,033,908	4,404,419
Prior years	<u>2,087,969</u>	<u>1,947,175</u>
Total paid	<u>8,121,877</u>	<u>6,351,594</u>
Balance, December 31	<u><u>\$ 2,071,323</u></u>	<u><u>\$ 3,026,055</u></u>

As a result of changes in estimates for anticipated losses and loss adjustment expenses to insured events of prior years, the liability for losses and loss adjustment expenses decreased by \$791,044 and \$219,489 in 2006 and 2005, respectively.

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**

Notes to Statutory Financial Statements, continued

For the years ended December 31, 2006

7. Lease Commitments:

The Facility conducts its operations in leased premises under a lease that will expire April 30, 2008. At December 31, 2006, minimum rental commitments under this noncancelable lease are as follows:

Year ending December 31:

2007	\$ 241,356
2008	<u>80,452</u>
 Total payments	 <u><u>\$ 321,808</u></u>

Total rental expense was \$271,358 and \$266,169 in 2006 and 2005, respectively.

Rentals included above are net of amounts allocated to the Insurance Placement Facility of Delaware and the West Virginia Essential Property Insurance Association for common facilities.

8. Related Party Transactions:

The Facility issues all checks for claims and other payables for the Insurance Placement Facility of Delaware and the West Virginia Essential Property Insurance Association, and is then reimbursed by these facilities. Throughout 2006 and 2005, \$864,717 and \$606,580, respectively, was paid on behalf of the Insurance Placement Facility of Delaware and \$1,018,288, and \$887,364, respectively, was paid on behalf of the West Virginia Essential Property Insurance Association. At December 31, 2006 and 2005, \$173,852 and \$50,686, respectively, is due from the Insurance Placement Facility of Delaware and \$63,089 and \$82,135, respectively, is due from the West Virginia Essential Property Insurance Association.

9. Annual Statement Reconciliation:

The following is a reconciliation between the accompanying statutory financial statements and the Annual Statement for the years ended December 31, 2006 and 2005:

	<u>2006</u>	
	<u>Net income</u>	<u>Members' equity</u>
As reported in the Annual Statement	\$ 2,157,262	\$ 2,518,127
2006 underwriting and other expense adjustment	<u>151,048</u>	<u>-</u>
 As reported herein	 <u><u>\$ 2,308,310</u></u>	 <u><u>\$ 2,518,127</u></u>

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Notes to Statutory Financial Statements, continued  
For the years ended December 31, 2006

9. Annual Statement Reconciliation, continued:

	2005	
	Net income	Members' deficit
As reported in the Annual Statement	\$ 2,669,790	\$ (205,069)
2005 underwriting and other expense adjustment	56,182	-
As reported herein	\$ 2,725,972	\$ (205,069)

The underwriting and other expense adjustments relate to the additional minimum pension liability adjustments discussed in Note 5.

**SUPPLEMENTAL SCHEDULES**

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
 Supplemental Investment Risk Interrogatories  
 December 31, 2006

Total admitted assets at December 31, 2006 \$14,290,839

1. State by investment category the 10 largest exposures to a single issuer/borrower/investment, excluding (i) U.S. government, U.S. government agency securities, and those U.S. government money market funds listed in the Appendix to the SVO Purposes and Procedures Manual as exempt; (ii) property occupied by the Company; and (iii) policy loans.

Investment category	Amount	Percentage of total admitted assets
None	\$ -	0.00%

2. State the amount and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

Bonds			Preferred stocks		
None	\$ -	0.00%	None	\$ -	0.00%

3. The Company holds no foreign investments.
4. The Company holds no Canadian investments.
5. The Company holds no investments with contractual sales restrictions.
6. State the amounts and percentages of admitted assets held in the largest 10 equity interests (including investments in shares of mutual funds, preferred stocks, publicly traded equity securities, and other equity securities, and excluding money market and bond mutual funds listed in the Appendix to the SVO Practices and Procedures Manual as exempt or Class 1).

Investment category	Amount	Percentage of total admitted assets
None	\$ -	0.00%

7. The Company holds no nonaffiliated, privately placed equities.

**INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA**  
Supplemental Investment Risk Interrogatories, continued  
December 31, 2006

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8. The Company holds no general partnership interests.
9. The Company holds no mortgage loans.
10. The Company holds no real estate.
11. The Company has no repurchase agreements.
12. The Company does not hold warrants.
13. The Company does not have exposure to collars, swaps, or forwards.
14. The Company does not have exposure for futures contracts.
15. The Company does not have amounts in the Write-Ins for Invested Assets category on the Summary Investment Schedule.

*See accompanying independent auditors' report.*

## INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA

## Summary of Investments

December 31, 2006

Investment categories	Gross investment holdings*		Admitted assets as reported in the annual statement	
Federal Home Loan Mortgage Association	\$ 9,904,008	70.71%	\$ 9,904,008	70.71%
Cash and cash equivalents	4,101,625	29.29%	4,101,625	29.29%
Total invested assets	<u>\$ 14,005,633</u>	<u>100.00%</u>	<u>\$ 14,005,633</u>	<u>100.00%</u>

\*Gross investment holdings as valued in compliance with NAIC Accounting Practices and Procedures Manual.

*See accompanying independent auditors' report.*

## INSURANCE PLACEMENT FACILITY OF PENNSYLVANIA

Reinsurance Interrogatories

December 31, 2006

Provided below are management's responses to certain reinsurance interrogatories required by NAIC Statutory Accounting Principles:

Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)? Yes ( ) No (X)

Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 3% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 3% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:

- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
- (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
- (c) Aggregate stop loss reinsurance coverage;
- (d) An unconditional or unilateral right by either party to commute the reinsurance contract, except for such provisions which are only triggered by a decline in the credit status of the other party;
- (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
- (f) Payment schedule, accumulating retentions from multiple years or any features inherently designed to delay timing of the reimbursement to the ceding entity.

Yes ( ) No (X)

Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), excluding cessions to approved pooling arrangements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:

- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
- (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates.

Yes ( ) No (X)

Except for transactions meeting the requirements of paragraph 30 of SSAP No. 62—Property and Casualty Reinsurance, disclose if the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:

- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles ("SAP") and as a deposit under generally accepted accounting principles ("GAAP"); or
- (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?

Yes ( ) No (X)