Annual Report 2009

Workers' Compensation Reinsurance Association®

WCRA®

30th Anniversary

To Our Members

2009: A Year of Recovery

When the WCRA was established by the Minnesota Legislature in 1979, it was charged with the responsibility of improving the long-term stability of the Minnesota workers' compensation system by providing reinsurance to help pay benefits for the state's catastrophically injured workers. Over the years, the Association has been successful in providing stable premium rates and high-quality service to its members and ultimately to injured workers. As we closed 2008, however, several factors combined to jeopardize the Association's ability to meet its long-term obligations. In response, the WCRA Board of Directors took several steps during 2009 that, coupled with significant positive returns in our investment portfolio, contributed to a substantial improvement in the Association's financial condition.

The Association is statutorily authorized to distribute surplus funds with approval from the Commissioners of the Minnesota Department of Labor and Industry and the Minnesota Department of Commerce. In accordance with this authority, in 1993, 1996, and 2000, we distributed a total of $1.23 billion to our members and to workers' compensation policyholders.

Conversely, if the WCRA accumulates a significant deficit, the Association is authorized to assess members and policyholders to strengthen its capital position. The surplus distributions noted above, combined with the 2008 global financial crisis, caused the WCRA's long-term financial condition to deteriorate. At year-end 2008, the deficit had grown to $424 million, nearly –30 percent of the Association's funded discounted reserves. After careful consideration, and following consultation with our regulators and many WCRA members, the Board of Directors approved a Surplus Distribution Recovery Program (Program) to assess WCRA members and workers' compensation policyholders a total of $268 million. The Program, which stipulated that these assessments would be collected over a five-year period beginning in 2010, was approved by our regulators on June 30, 2009.

Each member was given the option to prepay a portion of its five-year assessment amount in a lump sum at a discounted rate. Many members took advantage of that opportunity, and the Association received a total of $86 million in prepayments of Deficient Premiums Assessments in December 2009. For those members who did not prepay their assessments, the first of five regular installment payments of Deficient Premiums Assessments, as well as Deficiency Assessments payable by WCRA self-insurer members, will be due on July 15, 2010. In addition, WCRA insurer members began to collect Deficiency Assessments from their policyholders for renewals and new policies incepting on or after January 1, 2010. Insurer members will remit the collected Deficiency Assessments to the WCRA semiannually by August 1 and February 1 in each of the next five years.

The Board of Directors will review the Association's financial condition annually and is authorized to reduce or terminate the Program at any time if the Board determines that it is no longer necessary to collect the assessments. Additional details about the Program are available on the WCRA's website at www.wcra.biz.

The performance of the Association's investment portfolio is critical to the WCRA's financial well-being. We invest our assets in a way that reflects the long-term nature of the claims reported to the Association. Our discount rate, which is the expected rate of return on our invested assets, is 7 percent. Since the WCRA's inception in 1979, our annualized rate of return has been 10 percent, which was a key factor in building the surpluses that we distributed in previous years.

In 2008, however, our investments lost 27 percent. Some members suggested that the Association should immediately adopt a more conservative and less volatile investment strategy. Such a change, however, would have required us to lower our discount rate, which in turn would have significantly increased the size of our deficit; inhibited our ability to grow surplus through excess investment returns; and forced a substantial, permanent increase in premium rates. The Board of Directors concluded that we should stay the course. As a result, in 2009 our portfolio earned a record 30 percent rate of return, which contributed to the significant reduction in our deficit from $424 million to $199 million.

Operationally, the Association continued to focus on increasing its efficiency and improving services to members. As symbolized in the senior management photo included in this annual report, we are eliminating most paper records and converting all internal and claims documents to electronic files. In addition, the Board of Directors approved a policy requiring all members to submit claim reimbursement requests and loss reports electronically beginning January 1, 2010. The data collection for both the premium annual adjustment and self-insurer experience rating processes have been converted to electronic reporting. These and many other processes are being reviewed to identify methods to assist members, improve data quality, and reduce costs.

We want to take this opportunity to express our appreciation for the contributions of David Young, who completed his service on the Board of Directors in 2009. Dave was appointed to the Board in 2000 and provided outstanding leadership as its chair from 2002 to 2009.

As the WCRA commemorates its 30th anniversary, and we reflect upon the Association's mission and vision statements below, we also want to thank the WCRA membership and staff for their past and continued support of our commitment to the Minnesota workers' compensation system.

MISSION

The WCRA ensures the availability of long-term reinsurance protection for serious Minnesota workers' compensation claims. Our staff of innovative professionals is dedicated to achieving the highest standard of excellence through stable and reasonable rates, expert claims administration, and informational services.

VISION

The WCRA will provide reinsurance services that are considered superior by its members and other participants in the workers' compensation system.

Carl W. Cummins III
WCRA President and CEO

Stuart C. Henderson
WCRA Board Chair

2009 Financial Results
Management's Summary Analysis

Overview

The WCRA experienced significant financial improvement in 2009. The Association recorded comprehensive income of $189 million, a turnaround from the $390 million comprehensive loss recorded in 2008. At December 31, 2009, the balance sheet deficit was $199 million, an improvement of $225 million from the December 31, 2008 deficit of $424 million. This significant financial improvement was primarily due to a strong upturn in the domestic and international investment markets. The investment portfolio returned 30 percent in 2009 compared to a loss of 27 percent in 2008.

On May 19, 2009, the Board of Directors declared Deficient Premiums Assessments to members and Deficiency Assessments to self-insurer members and workers' compensation policyholders. These assessments were approved by the Association's regulators on June 30, 2009. In 2009, the WCRA recorded the first installment of $36 million of the Deficient Premiums Assessments as a contribution to capital. This contribution to capital also helped reduce the balance sheet deficit.

The WCRA's cash flow from operating activities was $4 million in 2009, compared to $36 million in 2008. This decrease was due primarily to two factors: a litigation settlement of $17 million in 2008 that did not repeat in 2009, and an increase in paid losses from $62 million in 2008 to $80 million in 2009. However, the WCRA has substantial liquidity and met all of its financial obligations on a timely basis in 2009.

Operating Results and Comprehensive Income

◆Premiums and Losses

The WCRA earned $55 million in funded premiums in 2009, up from $48 million in 2008. This increase was primarily due to an 18 percent increase in 2009 reinsurance rates.

Funded losses and loss expenses incurred for 2009 were $155 million, up significantly from $74 million in the prior year. This increase was due primarily to a significant reduction in 2008 actuarial adjustments of prior accident year losses. Prior accident year loss reserves were reduced by $2 million in 2009 compared to a reduction of $100 million in 2008. The significant reduction in prior accident year reserves in 2008 was due primarily to favorable development on case reserves, which resulted in lower projected ultimate losses.

The components of discounted funded losses and loss expenses incurred are shown below.

($ millions)	**2009**	**2008**
Prior accident years:		
Present value update	$ 98	$ 98
Actuarial adjustments	(2)	(100)
Total prior accident years	96	(2)
Current accident year	59	76
Total funded losses and loss expenses incurred	$155	$ 74

Investment Performance

For the year ended December 31, 2009, the investment portfolio returned 30 percent compared to a loss of 27 percent in 2008. The 2009 investment return was the best annual return in the history of the WCRA and was 23 percent above the 7 percent assumed rate of return. The 2009 investment performance was due to a strong upturn in the domestic and international investment markets. Returns on domestic equities, international equities, and fixed income investments all improved dramatically, driven by signs of global economic recovery. In 2009, the WCRA's domestic equities returned 27 percent, international equities returned 44 percent, and fixed income investments returned 25 percent. In 2008, domestic equities lost 38 percent, international equities lost 45 percent, and fixed income investments lost 3 percent.

The components of investment results are shown below.

($ millions)	**2009**	**2008**
Investment income, net of related expenses	$ 32	$ 36
Net realized investment (losses)	(23)	(148)
Change in unrealized gains (losses) on securities	282	(270)
Total investment results	$ 291	$(382)

In 2009 and 2008, the *WCRA Investment Policy* included asset allocation targets of 40 percent for domestic equities, 20 percent for international equities, and 40 percent for fixed income investments.

Comprehensive Income

The WCRA recorded a comprehensive income of $189 million in 2009, a significant turnaround from the comprehensive loss of $390 million recorded in 2008. Comprehensive income (loss) consists of net income (loss) and the change in unrealized gains (losses) on investments. In 2009, the comprehensive income was due primarily to strong investment performance, including unrealized investment gains totaling $282 million. In 2008, the comprehensive loss was due to the significant decline in the domestic and international investment markets.

Balance Sheet

Assets and Liabilities

Total assets were $1,611 million at December 31, 2009 compared with $1,469 million at the end of the previous year. The increase in total assets was due primarily to an increase in invested assets.

Total liabilities were $1,810 million at December 31, 2009 compared with liabilities of $1,893 million at December 31, 2008. The decrease in liabilities was due primarily to a decrease in the amount due to securities brokers for unsettled securities transactions.

The WCRA's largest liability is the reserve for funded losses and loss expenses, which totaled $1,512 million at December 31, 2009 compared with $1,436 million at December 31, 2008. This liability represents the present value, discounted at 7 percent, of the total estimated obligation for losses and loss expenses for unpaid amounts up to the prefunded limit. Because this liability involves claims that will be paid out over a period of many years, judgments as to the ultimate exposure are an important component of the loss reserving process. Reserves are reviewed on a regular basis using a variety of actuarial techniques. They are adjusted based on loss experience and as new information becomes available.

Changes in the discounted liability for funded losses and loss expenses are shown below.

($ millions)	**2009**	**2008**
Funded reserves as of January 1	$1,436	$1,426
Losses and loss expenses incurred:		
Prior accident years	96	(2)
Current accident year	59	76
Total incurred	155	74
Losses and loss expenses paid	(82)	(61)
Claims receivable from litigation settlement	3	(3)
Funded reserves as of December 31	$ 1,512	$1,436

The components of prior accident year incurred losses and loss expenses are discussed above under "Operating Results and Comprehensive Income."

The liability for unfunded losses and loss expenses totaled $180 million at December 31, 2009 compared to $164 million at December 31, 2008. This liability represents the present value, discounted at 7 percent, of the total estimated obligation for losses and loss expenses for unpaid amounts in excess of the prefunded limit. In 2009, the increase in this liability was driven by the present value update and reserves for the current accident year. In 2008, the decrease in this liability was due to a reduction in prior accident year loss reserves, which resulted from favorable case reserve development. Unfunded deferred premium revenue of $17 million was recognized in 2009, concurrent with incurred unfunded losses and loss expenses of $17 million. Loss payments in excess of prefunded limits totaled $1.3 million and $1.2 million in 2009 and 2008, respectively.

◆Deficit

At December 31, 2009, the WCRA had an accumulated deficit of $199 million, an improvement of $225 million from the December 31, 2008 deficit of $424 million. This improvement was primarily due to a strong upturn in the domestic and international investment markets. The investment portfolio returned 30 percent in 2009, well above the 7 percent assumed rate of return.

On May 19, 2009, the Board of Directors declared Deficient Premiums Assessments to members of $178 million and Deficiency Assessments to self-insurer members and workers' compensation policyholders of $90 million. The Deficient Premiums Assessments are payable in five equal annual installments beginning in 2010. In 2009, the WCRA recorded the first $36 million installment of the Deficient Premiums Assessments as a contribution to capital. This contribution to capital also helped reduce the balance sheet deficit. The Deficient Premiums Assessments are being recorded on an installment basis due to reasonable uncertainty regarding continuation of the assessments over the full five years. Whereas the Deficiency Assessments are prospective in nature and will be determined on a year-to-year basis over the next five years (2010–2014), they did not impact the deficit in 2009. The Deficiency Assessments will be recorded as an annual contribution to capital beginning in 2010.

CASH FLOW AND LIQUIDITY

Cash flow from operating activities was $4 million in 2009, compared to $36 million in 2008. This decrease was due primarily to two factors: a litigation settlement of $17 million in 2008 that did not repeat in 2009, and an increase in paid losses from $62 million in 2008 to $80 million in 2009. However, the WCRA has substantial liquidity and met all of its financial obligations on a timely basis in 2009. In addition, the WCRA has a marketable investment portfolio that can provide significant liquidity. Management believes the WCRA has the liquidity necessary to continue to meet its financial obligations on a timely basis for the foreseeable future.

WCRA Board of Directors

Back row, left to right

Raymond Waldron (Retired)
◆*Minnesota AFL-CIO*

Robert Lund
◆*SFM*

Gary Nelson
◆*Medtronic, Inc.*

Robert Ditmore
◆*The Travelers Companies, Inc.*

Howard Bicker
◆*Minnesota State Board of Investment*

David Hennes
◆*The Toro Company*

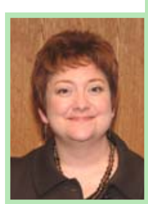
Front row, left to right

Edward Reynoso
◆*Teamsters Joint Council 32 DRIVE*

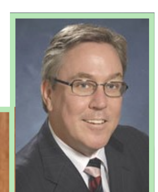
Allison Waggoner
◆*DCI, Inc.*

Stuart Henderson
◆*Western National Insurance Group*

Michele Spencer
◆*Ecumen*



Katherine Kardell
Minnesota Management and Budget◆



Brian Melas
◆*Liberty Mutual Insurance Group*

Wayne Simoneau
◆*Public Representative*

WCRA Senior Management

Left to right

Elisabeth Skoglund ◆ *Vice President – Claims and Information Systems*
James Heer ◆ *Vice President – Actuarial*
Donald Swanson ◆ *Vice President – Finance and Investments (WCRA Treasurer)*
Carl (Buzz) Cummins ◆ *President and Chief Executive Officer*
Cynthia Smith ◆ *Vice President – Operations (WCRA Secretary)*

Senior management poses above with a small sampling of the hundreds of boxes of member, claims, audit, and billing files that have been scanned and converted from paper format into electronic images. Since the commencement of this huge undertaking in 2006, the project has involved all WCRA departments.

The scanning of historical files, along with the direct conversion to electronic media of applicable paper documents received in the mail, now provides our staff with fast and efficient access to member and claims information from their computer screens. This conversion process, which is expected to be completed during 2010, has also produced significant savings in the Association's offsite storage and supply budgets, staff time, and office space requirements.

Although the WCRA will never be able to operate on a completely paperless basis, the electronic storage of documents, along with the transition to electronic reporting in the claims and premium areas, helps the Association continue to be a responsible, progressive, and environmentally conscious business partner.

Workers' Compensation Reinsurance Association

Financial Statements
December 31, 2009 and 2008

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Suite 1400
225 South Sixth Street
Minneapolis MN 55402
Telephone (612) 596 6000
Facsimile (612) 373 7160

Report of Independent Auditors

To the Board of Directors and Members of
Workers' Compensation Reinsurance Association

In our opinion, the accompanying balance sheets and the related statements of operations, comprehensive income (loss) and accumulated deficit and of cash flows present fairly, in all material respects, the financial position of the Workers' Compensation Reinsurance Association (the "Association") at December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. 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 of these statements 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, 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.

PricewaterhouseCoopers LLP

March 1, 2010

Workers' Compensation Reinsurance Association
Balance Sheets
December 31, 2009 and 2008

(in thousands of dollars)		2009		2008
Assets				
Investments, at fair value				
Cash and cash equivalents	**$**	**55,961**	$	121,156
Short-term		**1,657**		3,401
Securities lending collateral		**-**		63,717
Common and preferred stock		**816,559**		573,815
Bonds		**504,236**		420,441
Total investments		**1,378,413**		1,182,530
Uncollected reinsurance premiums				
Current premiums due		**20**		211
Deferred for unfunded losses		**179,612**		164,633
Total uncollected reinsurance premiums		**179,632**		164,844
Deficient premium assessments receivable (Note 9)		**15,920**		-
Accrued investment income		**4,207**		3,720
Due from securities brokers		**32,723**		117,527
Prepaid expenses and other assets		**386**		329
Property and equipment, less accumulated depreciation of $685 and $658 at December 31, 2009 and 2008, respectively		**80**		99
Total assets	**$**	**1,611,361**	$	1,469,049
Liabilities and Accumulated Deficit				
Liabilities				
Losses and loss expenses				
Funded	**$**	**1,511,871**	$	1,435,549
Unfunded		**179,990**		164,372
Total losses and loss expenses		**1,691,861**		1,599,921
Payable under securities loan agreement		**-**		76,021
Deferred deficient premium assessments (Note 9)		**66,333**		-
Due to securities brokers		**50,758**		215,711
Accounts payable and other liabilities		**987**		1,091
Total liabilities		**1,809,939**		1,892,744
Accumulated deficit from operations		**(347,498)**		(290,748)
Accumulated other comprehensive income (loss)		**148,920**		(132,947)
Designated accumulated deficit		**(198,578)**		(423,695)
Total liabilities and accumulated deficit	**$**	**1,611,361**	$	1,469,049

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

Workers’ Compensation Reinsurance Association
Statements of Operations, Comprehensive Income (Loss) and Accumulated Deficit
Years Ended December 31, 2009 and 2008

(in thousands of dollars)		**2009**		**2008**
Revenues				
Reinsurance premiums				
Funded earned	**$**	**54,804**	$	47,523
Unfunded deferred		**16,920**		(17,467)
Investment income, net of related expenses		**31,866**		36,229
Realized investment (losses)				
Net realized investment (losses)		**(18,222)**		(62,057)
Net realized impairment (losses)		**(4,384)**		(86,142)
Litigation settlement income (Note 10)		**-**		20,000
Total revenues		**80,984**		(61,914)
Expenses				
Losses and loss expenses				
Funded		**154,700**		73,683
Unfunded		**16,920**		(17,467)
Losses and loss expenses incurred		**171,620**		56,216
Operating and administrative expenses		**1,900**		2,140
Total expenses		**173,520**		58,356
Net loss		**(92,536)**		(120,270)
Other comprehensive income (loss)				
Change in net unrealized gains (losses) on securities and foreign currency translation adjustment		**281,867**		(270,048)
Comprehensive income (loss)		**189,331**		(390,318)
Deficient premium assessments (Note 9)		**35,786**		-
Accumulated deficit, beginning of year		**(423,695)**		(33,377)
Accumulated deficit, end of year	**$**	**(198,578)**	$	(423,695)

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

Workers' Compensation Reinsurance Association
Statements of Cash Flows
Years Ended December 31, 2009 and 2008

(in thousands of dollars)		**2009**		**2008**
Cash flows from operating activities				
Net premiums collected	**$**	**55,503**	$	47,791
Interest and dividends received, net of related expenses		**30,333**		36,755
Litigation settlement received (Note 10)		**-**		16,614
Losses and loss expenses paid		**(79,680)**		(62,195)
Operating and administrative expenses paid		**(2,193)**		(2,692)
Net cash provided by operating activities		**3,963**		36,273
Cash flows from investing activities				
Sale of investments				
Collateral for securities on loan, net		**63,717**		187,956
Common and preferred stocks		**822,503**		427,357
Bonds		**3,461,832**		2,873,657
Purchase of investments				
Short-term		**(1,744)**		(771)
Common and preferred stocks		**(885,282)**		(535,194)
Bonds		**(3,538,423)**		(2,719,246)
Purchase of equipment		**(8)**		(72)
Net cash provided by (used in) investing activities		**(77,405)**		233,687
Cash flows from financing activities				
Payable under securities loan agreement		**(76,021)**		(187,956)
Deficient premium assessments		**84,268**		-
Net cash provided by (used in) financing activities		**8,247**		(187,956)
Net (decrease) increase in cash and cash equivalents		**(65,195)**		82,004
Cash and cash equivalents				
Beginning of year		**121,156**		39,152
End of year	**$**	**55,961**	$	121,156

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

1. General Information

Description of Association

In 1979, the Minnesota Legislature created the Workers' Compensation Reinsurance Association (the "Association"), a nonprofit, unincorporated association, to provide reinsurance protection for serious workers' compensation losses to all primary workers' compensation insurance providers and self-insured employers in the state of Minnesota. The Association provides full indemnification to its members for workers' compensation losses paid in accordance with Minnesota Statutes Chapter 176 that exceed a member's retention limit.

Operating procedures are prescribed by Minnesota Statutes Section 79.34-79.40, as amended (the "Enabling Act"), and the Association's Plan of Operation (the "Plan"). Amendments to the Plan must be approved by the Board of Directors of the Association (the "Board") and the Minnesota Commissioner of Labor and Industry.

Membership

All insurance carriers authorized to underwrite workers' compensation risks in Minnesota and all employers, including political sub-divisions, authorized to self-insure their workers' compensation liabilities in Minnesota are required to be members of the Association.

Retention Limits

For 2009, members selected one of three maximum per-loss occurrence retention limits, which were $430,000, $860,000 or $1,720,000. For 2008, members selected one of three maximum per-loss occurrence retention limits, which were $410,000, $820,000 or $1,640,000. Retention limits are determined annually based on a formula prescribed in the Enabling Act. Minnesota workers' compensation losses incurred by members in excess of the retention limit selected are reinsured by the Association.

Premiums

The estimated aggregate annual reinsurance premium billed by the Association to members in each calendar year is calculated to cover the following estimated costs:

- The present value of the estimated ultimate liability for members' incurred losses above the selected retention limit up to and including the prefunded limit of $8.6 million and $8.2 million per occurrence for 2009 and 2008, respectively, for funded losses reinsured by the Association.

- Loss payments expected to be made to members for claim amounts in excess of prefunded limits (unfunded losses).

- Operating and administrative expenses of the Association, and loss expenses incurred by the Association. (Loss expenses incurred by members on reinsured claims are not recoverable from the Association.)

- Charges for the current year or a prior year, as determined by the Board, for any reinsurance coverage purchased by the Association.

- Adjustments due to excess or deficient funded premiums, if any, for prior years as determined by the Board.

Estimated reinsurance premiums for each year are billed to the individual members based on: (1) the funded rate for the member's selected retention limit; (2) the rate for expected unfunded payments; and (3) the member's most recent actual exposure base available at the beginning of the annual billing cycle, adjusted for a factor which represents the estimated difference between the member's most recent actual exposure base and the actuarially projected exposure base. In the following year, reinsurance premium adjustments to bring the estimated premiums to actual are calculated and billed or credited to members. In addition, members may be charged for reinsurance purchased by the Association based on: (1) the rate for the reinsurance protection and (2) the member's estimated or actual exposure base for the coverage year of the reinsurance protection.

For insurer members, the exposure base is the earned premium at the designated statistical reporting level reported in the Annual Financial Call for Experience to the Minnesota Workers' Compensation Insurers Association ("MWCIA") multiplied by 1.20. Experience rating modifications of the insurers' individual insureds are reflected in the Annual Call data.

For self-insurer members, the exposure base is calculated from Minnesota's covered payroll, multiplied by pure premium base rates as published by the MWCIA, multiplied by 1.20, multiplied by an experience rating modification factor.

2. Summary of Significant Accounting Policies

Use of Estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Risks and Uncertainties
The Association invests in stocks and bonds of U.S. and foreign companies, U.S. government securities, and mortgage-backed securities. The investment viability and return of funds is dependent on, among other factors, the financial results of the underlying issuers. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the values will occur in the near term and that such changes could materially affect the financial statements.

The process of estimating the liability for losses and loss expenses, by its very nature, involves substantial uncertainty. The level of uncertainty is influenced by factors such as the economic assumptions associated with workers' compensation reinsurance. Ultimate actual payments for losses and loss expenses could be significantly different from the estimates.

Comprehensive Income
The Association follows the reporting concept of "Comprehensive Income" which requires the reporting of comprehensive income in addition to net income from operations. Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income. Comprehensive income for the Association includes net income and other comprehensive income, which includes unrealized gains and losses on available-for-sale securities, the impact of foreign currency translation adjustments on securities denominated in a currency other than U.S. dollars, and the change in the funded status of the defined benefit pension plan.

Cash Equivalents
Cash on deposit, shares in money market funds, and short-term debt securities with original maturities of three months or less are classified as cash equivalents.

Short-Term
Debt securities with original maturities greater than three months and less than one year are classified as short term. Amortized cost approximates market value.

Investments
The Association has classified its investments as “available for sale” and carries such securities at fair value. Accordingly, the net unrealized gains or losses are included in other comprehensive income as a separate component of surplus. In determining the realized gain or loss on sales of investments, cost is based on the average cost method. Interest income is recognized when earned. Dividend income is recognized on the ex-dividend date.

Purchased premiums and discounts are amortized or accreted using the effective interest rate method over the terms of the respective issues.

When a decline in value of an investment is determined to be other than temporary, the specific investment is carried at estimated fair value, and its original book value is reduced to reflect this impairment. Such reductions in book value are recognized in the period in which they were written down as either realized investment losses or as a component of other comprehensive income. See also “New Accounting Pronouncements” in Note 2 and Note 3.

Effective January 1, 2008, the Association adopted Accounting Standards Codification (“ASC”) 820. This Standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2: Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The fair value disclosures in Note 7 have been expanded in accordance with this Standard.

Property and Equipment
Property and equipment are stated at cost. Depreciation on property and equipment is calculated on the straight-line method over the estimated useful lives of the assets. Upon sale or retirement of property and equipment, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is credited or charged to operations.

Determination of Required Capital
After the close of each fiscal year or at such other times that it deems appropriate, the Board reports whether capital or a deficit exists based on the annual audited year-end financial statements. In determining whether or not to declare an excess surplus distribution or a deficiency assessment, the Board evaluates the capital or deficit relative to the reserves for discounted funded

losses and loss expenses. The Board has determined that up to 60% of the liability for funded losses and loss expenses should be retained and reflected on the balance sheet as required capital. Required capital is needed to maintain sufficient assets to provide for variations between expected and actual investment returns, variations between expected and actual claims experience, and other unexpected financial developments. The Board will consider a deficiency assessment if the designated accumulated deficit exceeds 10% of the liability for funded losses and loss expenses.

The Board may declare an excess surplus distribution or an assessment if no such distribution or assessment has been declared in the preceding four years, provided that distributions or assessments may be declared more or less frequently than every five years if the Board, at its sole discretion, determines that it is necessary and prudent to do so. Excess surplus distributions or assessments may be declared by the Board and distributed to or collected from members or policyholders pursuant to the provisions of The Enabling Act and applicable provisions of the Plan. In 2009, the Board declared deficient premium assessments and deficiency assessments. See also Note 9.

Reinsurance Premiums
Funded earned reinsurance premiums are for the calendar year coverage period for funded losses (losses up to and including the prefunded limit). These premiums are billed in the current period. The reinsurance premiums for the calendar year may also include a credit or charge to equitably distribute excess or deficient premiums for previous periods, including any excess or deficient premiums resulting from a retroactive change in the prefunded limit.

Unfunded deferred reinsurance premiums are to be billed in future years for unfunded losses (loss amounts in excess of the prefunded limit) incurred during the calendar year coverage period and are recognized as earned revenue concurrent with the related unfunded losses and loss expenses. Reinsurance premiums for unfunded losses are billed to the members of the Association in the calendar year when payments in excess of prefunded limits are expected to be reimbursed by the Association. The Association began billing for losses in the unfunded layer in 2003. Premiums of $1,940,000 and $854,000 were billed in 2009 and 2008, respectively.

Losses and Loss Expenses
The liability for funded losses and loss expenses represents the present value, discounted using 7%, of the estimated liability for losses and loss expenses of the Association for unpaid amounts up to and including the prefunded limit, as determined by actuarial projections using historical pricing model simulations and the payment and case reserve experience of the Association.

The liability for unfunded losses and loss expenses represents the present value, discounted using 7%, of the estimated liability for losses and loss expenses of the Association for unpaid amounts in excess of the prefunded limit, as determined by actuarial projections of the Association.

Subsequent Events
The Association has evaluated events that have occurred subsequent to December 31, 2009, through March 1, 2010, the date these financial statements were issued, and has determined that all material events have been properly recorded and disclosed.

New Accounting Pronouncements
Effective January 1, 2009, the Association adopted the provisions of FASB Accounting Standards Codification ASC 815-10-50. These new provisions amend and expand the disclosure requirements related to derivative instruments, to provide users of financial statements with an

enhanced understanding of the use of derivative instruments by the Association and how these derivatives affect the financial position, financial performance and cash flows of the Association. This Statement requires qualitative disclosures about the objectives and strategies for using derivative instruments, quantitative disclosures about the fair value of, and gains and losses on derivative instruments, as well as disclosures about credit-risk-related contingent features in derivative agreements. Note 3 includes the expanded derivative disclosures in accordance with ASC 815-10-50.

In April 2009, the FASB updated the accounting standards for the recognition and presentation of other-than-temporary impairments. The standard amends existing guidance on other-than-temporary impairments for debt securities. Impairment is now considered to be other-than-temporary if the entity (1) intends to sell the security, (2) more likely than not will be required to sell the security before recovering its cost, or (3) does not expect to recover the security's entire amortized cost basis (even if the entity does not intend to sell). If the entity does not intend to sell the impaired debt security and is not likely to be required to sell before recovery, the entity must determine the portion of the impairment that is due to credit loss and the portion that relates to all other factors. A credit loss is determined by comparing the best estimate of the cash flows expected to be collected from a security with the amortized cost of the security. The credit loss portion of the loss is recognized in earnings and the remainder of the loss is recognized in other comprehensive income. This standard is effective for annual reporting periods ending after June 15, 2009. The Association adopted the standard in 2009 and the additional disclosures are included in Note 3.

In December 2008, the FASB updated the accounting standards to require enhanced disclosure related to postretirement benefit plan assets, including information about inputs used to determine the fair value of plan assets. The standard is effective for the fiscal years ending after December 15, 2009. The Association adopted this standard as of December 31, 2009, and the expanded disclosures are included in Note 5.

3. Investments

The cost of common and preferred stocks, amortized cost of bonds, and estimated fair values at December 31, 2009 and 2008, are as follows:

	2009			
(in thousands of dollars)	**Cost/ Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Estimated Fair Value**
Short-term	**$ 1,914**	**$ -**	**$ (257)**	**$ 1,657**
Common stocks	**$ 694,974**	**$ 126,000**	**$ (10,101)**	**$ 810,873**
Preferred stocks	**5,184**	**807**	**(305)**	**5,686**
Total stocks	**$ 700,158**	**$ 126,807**	**$ (10,406)**	**$ 816,559**
U.S. Treasury securities and obligations of U.S. government and agencies	**$ 154,865**	**$ 1,767**	**$ (2,715)**	**$ 153,917**
Corporate debt securities	**233,539**	**36,355**	**(3,061)**	**266,833**
Mortgage-backed securities	**82,173**	**1,749**	**(436)**	**83,486**
Total bonds	**$ 470,577**	**$ 39,871**	**$ (6,212)**	**$ 504,236**

	2008							
(in thousands of dollars)		**Cost/ Amortized Cost**		**Gross Unrealized Gains**		**Gross Unrealized Losses**		**Estimated Fair Value**
Short-term	$	3,404	$	-	$	(3)	$	3,401
Securities lending collateral		66,795		-		(3,078)		63,717
Common stocks	$	687,017	$	24,769	$	(144,757)	$	567,029
Preferred stocks		7,374		208		(796)		6,786
Total stocks	$	694,391	$	24,977	$	(145,553)	$	573,815
U.S. Treasury securities and obligations of U.S. government and agencies	$	86,315	$	2,180	$	(5,934)	$	82,561
Corporate debt securities		199,271		9,445		(15,716)		193,000
Mortgage-backed securities		143,421		1,614		(155)		144,880
Total bonds	$	429,007	$	13,239	$	(21,805)	$	420,441

Total unrealized losses were $16.9 million and $170.4 million at December 31, 2009 and 2008, respectively. The following tables provide a breakdown of unrealized losses at December 31, 2009 and 2008. The Association has reviewed the components and duration of these unrealized losses and concluded that the losses are temporary in nature. The unrealized losses are primarily on common stocks. The unrealized losses as of December 31, 2009 and 2008, are as follows:

	Unrealized Holding Losses as of December 31, 2009											
	Less than 12 months				**12 months or more**				**Total**			
(in thousands of dollars)		**Estimated Fair Value**		**Unrealized Losses**		**Estimated Fair Value**		**Unrealized Losses**		**Estimated Fair Value**		**Unrealized Losses**
Short-term	**$**	**1,657**	**$**	**(257)**	**$**	**-**	**$**	**-**	**$**	**1,657**	**$**	**(257)**
Common stocks	**$**	**47,541**	**$**	**(3,203)**	**$**	**50,280**	**$**	**(6,898)**	**$**	**97,821**	**$**	**(10,101)**
Preferred stocks		**2,381**		**(305)**		**-**		**-**		**2,381**		**(305)**
Total stocks	**$**	**49,922**	**$**	**(3,508)**	**$**	**50,280**	**$**	**(6,898)**	**$**	**100,202**	**$**	**(10,406)**
U.S. Treasury securities and obligations of U.S. government and agencies	**$**	**114,882**	**$**	**(2,715)**	**$**	**-**	**$**	**-**	**$**	**114,882**	**$**	**(2,715)**
Corporate debt securities		**27,499**		**(746)**		**20,220**		**(2,315)**		**47,719**		**(3,061)**
Mortgage-backed securities		**38,603**		**(430)**		**302**		**(6)**		**38,905**		**(436)**
Total bonds	**$**	**180,984**	**$**	**(3,891)**	**$**	**20,522**	**$**	**(2,321)**	**$**	**201,506**	**$**	**(6,212)**

	Unrealized Holding Losses as of December 31, 2008					
	Less than 12 months		12 months or more		Total	
(in thousands of dollars)	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Short-term	$ 3,401	$ (3)	$ -	$ -	$ 3,401	$ (3)
Securities lending collateral	63,717	(3,078)	-	-	63,717	(3,078)
Common stocks	$ 273,705	$ (83,688)	$ 106,913	$ (61,069)	$ 380,618	$ (144,757)
Preferred stocks	2,280	(796)	-	-	2,280	(796)
Total stocks	$ 275,985	$ (84,484)	$ 106,913	$ (61,069)	$ 382,898	$ (145,553)
U.S. Treasury securities and obligations of U.S. government and agencies	$ 19,764	$ (5,747)	$ 1,833	$ (187)	$ 21,597	$ (5,934)
Corporate debt securities	91,189	(12,756)	17,429	(2,960)	108,618	(15,716)
Mortgage-backed securities	16,884	(151)	774	(4)	17,658	(155)
Total bonds	$ 127,837	$ (18,654)	$ 20,036	$ (3,151)	$ 147,873	$ (21,805)

The amortized cost and estimated fair value of debt securities at December 31, 2009, by contractual maturity, are shown below:

(in thousands of dollars)	Amortized Cost	Estimated Fair Value
Due in one year or less	**$ 9,625**	$ 11,262
Due after one year through five years	**90,796**	91,409
Due after five years through ten years	**105,389**	105,340
Due after ten years	**264,767**	296,225
	$ 470,577	$ 504,236

Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

The Association evaluates its investment securities for other-than-temporary impairment on an annual basis. Factors considered in determining whether an impairment is other-than-temporary include: 1) the length of time and the extent to which fair value is less than cost, 2) the financial condition, industry, and near-term prospects of the issuer, 3) adverse changes or events impacting the issuer, and 4) for equity securities, the ability and intent of the Association to hold these investments until recovery.

During 2009, the Association made a determination that the decline in the fair value of certain of its investments was other than temporary. As a result of this determination, the cost bases of the individual securities were written down to fair value as the new cost bases. For debt securities, the Association further determined that the decline in fair value that was other-than-temporary was entirely credit loss. In 2009, the total write-down for all investments was $4.4 million and this entire amount was recorded in earnings as a realized loss. The Association also wrote down $77.4 million of individual securities to fair value in 2008.

Other comprehensive loss in 2009 and 2008 is comprised of the change in unrealized gains (losses) on available-for-sale securities arising during the year, the impact of foreign currency translation adjustments on securities denominated in currency other than U.S. dollars and the change on the funded status of the defined benefit pension plan as follows:

(in thousands of dollars)		2009		2008
Change in net unrealized losses on securities	**$**	**277,888**	$	(256,329)
Foreign currency net translation gain (loss)		**4,138**		(13,247)
Pension benefit obligation		**(159)**		(472)
Total other comprehensive income (loss)	**$**	**281,867**	$	(270,048)

(in thousands of dollars)		2009		2008
Accumulated other comprehensive income (loss) consists of				
Net unrealized gains (losses) on securities	**$**	**145,915**	$	(131,973)
Foreign currency translation gain (loss)		**3,888**		(250)
Pension benefit obligation		**(883)**		(724)
Total accumulated other comprehensive income (loss)	**$**	**148,920**	$	(132,947)

Gross gains of $238.8 million and $197.0 million, and gross losses of $257.0 million and $259.1 million, were realized on sales of investments during 2009 and 2008, respectively. Additional realized losses of $4.4 million and $86.1 million were recognized due to other than temporary impairment of securities during 2009 and 2008, respectively. Net investment income and net realized investment (losses) gains during the years ended December 31, 2009 and 2008, are summarized below:

	Net Investment Income				Net Realized (Losses) Gains			
(in thousands of dollars)		2009		2008		2009		2008
Cash and cash equivalents	**$**	**270**	$	1,471	**$**	**1**	$	8,702
Common and preferred stocks		**11,832**		13,315		**(56,248)**		(102,166)
Bonds		**24,716**		25,790		**33,641**		(45,951)
Securities lending		**175**		6,276		**-**		(8,784)
Miscellaneous		**109**		150		**-**		-
		37,102		47,002	**$**	**(22,606)**	$	(148,199)
Investment expenses		**(5,137)**		(5,262)				
Securities lending interest expense		**(80)**		(5,335)				
Securities lending bank fees		**(19)**		(176)				
	$	**31,866**	$	36,229				

In 2009, net realized losses consisted of losses on securities of approximately $23 million and foreign currency translation gain of $.3 million. In 2008, net realized losses consisted of losses on securities of approximately $157 million and foreign currency translation gain of $9 million.

The Association terminated participation in the Wells Fargo securities lending program in March 2009. All securities loans were terminated and all obligations to borrowing brokers were settled. At December 31, 2008, the Association had equity and fixed income securities with fair values of approximately $75 million on loan.

While participating in the securities loan program, the Association reflected the collateral received for securities on loan on the balance sheet. An asset of approximately $64 million and the related liability representing the collateral received of $76 million are reflected on the balance sheet at December 31, 2008. In 2008, the Association made a determination that a decline in the fair value of certain collateral investments was other-than-temporary, and a write down of approximately $8.8 million was recorded in earnings as realized losses. In addition, an unrealized loss of $2.2 million was recorded in 2008 to reflect a decline in fair value of collateral investments believed to be temporary. See also Note 10, Contingencies.

The new FASB accounting standard ASC 815-105-50 expands the disclosure requirements for derivative instruments and related hedging activities. However, the adoption of the standard had no impact on the Balance Sheets, Statements of Operations and Comprehensive Income (Loss), or the Statements of Cash Flows. The Association has entered into interest-rate future, stock index future, interest-rate options, and interest rate swap contracts. These derivatives are used for several purposes including the management of yield curve and duration on fixed income investments, and for the overlay of cash balances to maintain equity and fixed income exposure in accordance with asset allocation policy. Hedge accounting is not used for any derivative contracts. The primary risks of these derivative instruments are interest rate, credit, and equity market risk. By using certain derivative instruments, the Association is exposed to the counterparty's credit risk i.e. the risk that derivative counterparties may not perform in accordance with the contractual provisions. The Association's exposure to counterparty credit risk is limited to the unrealized gains on such transactions. As of December 31, 2009, the total fair value of derivative instruments was less than 1% of the total investments. In 2009, net realized losses and the change in net unrealized gains on derivatives totaled less than 1% of comprehensive income.

4. Liabilities for Losses and Loss Expenses

The liability for losses and loss expenses at December 31, 2009 and 2008, is summarized as follows:

(in thousands of dollars)	**2009**	**2008**
Funded, undiscounted	**$ 6,409,177**	$ 5,778,591
Discount	**(4,897,306)**	(4,339,656)
Claims receivable from litigation settlement (Note 10)	**-**	(3,386)
Funded, discounted	**1,511,871**	1,435,549
Unfunded, undiscounted	**1,554,652**	1,449,533
Discount	**(1,374,662)**	(1,285,161)
Unfunded, discounted	**179,990**	164,372
Total, discounted	**$ 1,691,861**	$ 1,599,921

Funded Liabilities

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

(in thousands of dollars)	**2009**	**2008**
Balance at January 1		
Funded, undiscounted	**$ 5,778,591**	$ 5,749,270
Incurred related to		
Current year	**382,496**	404,077
Prior years	**329,854**	(313,786)
Total incurred	**712,350**	90,291
Paid related to		
Current year	**1,454**	187
Prior years	**80,310**	60,783
Total paid	**81,764**	60,970
Balance at December 31		
Funded, undiscounted	**6,409,177**	5,778,591
Discount	**(4,897,306)**	(4,339,656)
Claims receivable from litigation settlement (Note 10)	**-**	(3,386)
Funded, discounted	**$ 1,511,871**	$ 1,435,549

Reserves are reviewed periodically and updated based on current claims experience, trends, and economic outlook.

The following table compares the present value of the Association's funded reserve changes during 2009 with those of 2008.

	2009	**2008**
Discount rate at year end	**7.0%**	**7.0%**

(in thousands of dollars)	**2009**	**2008**
Funded reserves as of prior year end	**$ 1,435,549**	$ 1,426,221
Prior year impact of actuarial adjustments	**(2,141)**	(100,357)
Payments on prior accident years	**(80,310)**	(60,783)
Present value update	**97,915**	97,708
Reserves for current accident year	**57,472**	76,146
Total calendar year funded reserve changes	**72,936**	12,714
Claims receivable from litigation settlement (Note 10)	**3,386**	(3,386)
Funded reserves as of year end	**$ 1,511,871**	$ 1,435,549

In 2008, the significant reduction in prior year loss reserves was due primarily to favorable development on case-incurred losses. This favorable case development resulted in lower projected ultimate losses for all three retention levels.

Unfunded Liabilities

Payments on prior accident years in excess of prefunded limits totaled $1,302,000 and $1,225,000 in 2009 and 2008, respectively. Anticipated payments in excess of prefunded limits are billed as premiums for the unfunded layer.

The unfunded reserve methodology follows the funded analysis. Discount rates for unfunded reserves are the same as the funded reserves. The table below compares the present value unfunded reserve changes during 2009 with those of 2008.

(in thousands of dollars)	**2009**	**2008**
Unfunded reserves as of prior year end	**$ 164,372**	$ 183,064
Prior year changes		
Prior year impact of actuarial adjustments	**-**	(35,654)
Payments on prior accident years	**(1,302)**	(1,225)
Present value update	**11,461**	12,772
Reserves for the current accident year	**5,459**	5,415
Total calendar year unfunded reserve changes	**15,618**	(18,692)
Unfunded reserves as of year end	**$ 179,990**	$ 164,372

In 2008, favorable development on case-incurred losses resulted in a reduction in the unfunded liabilities. This favorable case development resulted in lower projected ultimate losses.

Reserve changes for the unfunded layer do not have an impact on accumulated deficit because on the statement of operations, unfunded losses incurred (which include reserve changes) are offset by an unfunded deferred premium.

5. Employee Benefit Plans

Defined Benefit Pension Plan

The Association has a non-contributory defined benefit pension plan that covers employees who meet eligibility and entry date requirements. The Association uses a December 31 measurement date. As of December 31, 2009, the plan's investment mix was 60% equities and 40% debt securities. The determination of the long-term rate of return on plan assets was based on historical rates of return and future estimated returns for the individual assets classes. Based on the target allocation, the overall expected long-term rate of return for the plan is 8%.

Benefits paid in 2009 were $79,502. The estimated benefit payments for 2010 are $23,106.

(in thousands of dollars)	**2009**	**2008**
Benefit obligation, end of year	**$ 2,672**	**$** 1,982
Plan assets at fair value, end of year	**2,099**	1,258
Funded status (recognized as a component of accrued liabilities and accumulated comprehensive income)	**$ (573)**	**$** (724)

(in thousands of dollars)		**2009**		**2008**
Employer contributions	**$**	**523**	**$**	135
Discount rate		**5.86%**		6.70%
Expected return on plan assets		**8.00%**		8.00%
Rate of compensation increase		**4.00%**		4.00%

The fair value of the plan's assets was determined in accordance with ASC 820, Fair Value Measurements, using the three levels of inputs described in Note 2.

The fair value of plan equities of $1.3 million was determined using Level 1 inputs consisting of quoted prices for identical securities in active markets. The fair value of plan debt securities of $0.8 million was determined using Level 2 inputs consisting of quoted prices for similar securities in active markets. There were no securities where the fair value was determined using Level 3 inputs, i.e. unobservable inputs supported by little or no market activity.

Defined Contribution Plan

The Association sponsors a defined contribution plan, which covers employees who meet the plan's eligibility requirements and have completed the service requirements, under Section 401(k) of the Internal Revenue Code. Participants can contribute a certain percentage of their compensation (subject to annual contribution limits) to the plan. In 2009 and 2008, the Association matched a maximum of 6% of participant eligible compensation. The Association's matching contribution to the plan was $0.1 million and $0.1 million in 2009 and 2008, respectively.

6. Income Tax Status

In 1996, the Association was granted an exemption from federal income taxes under Section 501(c)(27)(a) of the Internal Revenue Code. The Association received a tax-exempt determination letter from the Internal Revenue Service dated February 7, 1997. Therefore, no provision for income taxes is included in the Association's financial statements.

7. Fair Value Measurements

Accounting Standards Codification 820 defines fair value as the exit price that would be received for an asset in the principal or most advantageous market for the asset. See Note 2 for the three levels of inputs that may be used in measuring fair value. The fair value of the $959.6 million and $642.5 million of the investment securities as of December 31, 2009 and 2008, respectively, was determined using Level 1 inputs consisting of quoted prices for identical securities in active markets. The fair value of the $362.8 million and $418.9 million of the investment securities as of December 31, 2009 and 2008, respectively, was determined using Level 2 inputs consisting of quoted prices for similar securities in active markets. There were no securities as of December 31, 2009 and 2008, respectively, where the fair value was determined using Level 3 inputs, i.e. unobservable inputs supported by little or no market activity.

Assets measured at fair value are summarized below:

(in thousands of dollars)	**Fair Value Measurement Using**			
As of December 31, 2009	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Short-term	**$ -**	**$ 1,657**	**$ -**	**$ 1,657**
Common stocks	**$ 810,873**	**$ -**	**$ -**	**$ 810,873**
Preferred stocks	**-**	**5,686**	**-**	**5,686**
Total stocks	**$ 810,873**	**$ 5,686**	**$ -**	**$ 816,559**
U.S. Treasury securities and obligations of U.S. government and agencies	**$ 148,774**	**$ 5,143**	**$ -**	**$ 153,917**
Corporate debt securities	**-**	**266,833**	**-**	**266,833**
Mortgage-backed securities	**-**	**83,486**	**-**	**83,486**
Total bonds	**$ 148,774**	**$ 355,462**	**$ -**	**$ 504,236**

(in thousands of dollars)	**Fair Value Measurement Using**			
As of December 31, 2008	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Short-term	$ -	$ 3,401	$ -	$ 3,401
Securities lending collateral	-	63,717	-	63,717
Common stocks	$ 567,029	$ -	$ -	$ 567,029
Preferred stocks	-	6,786	-	6,786
Total stocks	$ 567,029	$ 6,786	$ -	$ 573,815
U.S. Treasury securities and obligations of U.S. government and agencies	$ 75,463	$ 7,098	$ -	$ 82,561
Corporate debt securities	-	193,000	-	193,000
Mortgage-backed securities	-	144,880	-	144,880
Total bonds	$ 75,463	$ 344,978	$ -	$ 420,441

8. Cash Flows and Liquidity

A reconciliation of net loss to net cash provided by operating activities for the years ended December 31, 2009 and 2008, is as follows:

(in thousands of dollars)	**2009**	**2008**
Net loss	**$ (92,536)**	$ (120,270)
Adjustments to reconcile net loss to net cash provided by operating activities		
Net realized investment losses (gains)	**22,606**	148,199
Decrease (increase) in claims receivable from litigation settlement	**3,386**	(3,386)
(Increase) decrease in funded uncollected reinsurance premiums, net of accrued premium adjustments	**(1,624)**	586
Increase in liability for funded losses and loss expenses	**76,322**	9,328
Other, net	**(4,191)**	1,816
Total adjustments	**96,499**	156,543
Net cash provided by operating activities	**$ 3,963**	$ 36,273

In 2008, as a result of overall investment market conditions, the Association incurred significant investment losses. These investment losses resulted in a significant increase in the comprehensive loss and the accumulated deficit. In 2009, the investment markets improved significantly, and the Association recovered a substantial portion of the losses incurred in 2008. The Association has substantial liquidity and a marketable investment portfolio that can provide significant liquidity. During 2009 and 2008, the Association met all of its financial obligations on a timely basis and management believes that it has the liquidity necessary to continue to do so for the foreseeable future.

9. Assessments

On May 19, 2009 the Board declared deficient premium assessments to members of $178 million and deficiency assessments to self-insurer members and workers' compensation policyholders of $90 million.

Deficient Premium Assessments
The deficient premium assessments are retrospective in nature, and are based on members' historic WCRA exposures and selected coverage layers from 1979 to 2008. All insurers and self-insurers who were members of the WCRA on December 31, 2008, are obligated to pay deficient premium assessments.

The deficient premium assessments are payable in five equal annual installments, with the first installment due on July 15, 2010, and subsequent installments due on each January 15, from 2011 through 2014. Members were given the options of prepaying their entire five-year deficient premium assessment on either December 1, 2009 or July 15, 2010, and having the assessment obligation discounted at an annual rate of 7%.

In 2009, the Association recorded the first installment of $35.8 million of the deficient premium assessments as a contribution to capital. The deficient premium assessments are being recorded on an installment basis due to reasonable uncertainty regarding continuation of the assessments over the full five years. The Board Resolution declaring the assessments provides that annually the Board will determine whether additional capital produced by earlier assessments, improved investment performance, and/or adjustments in loss reserve requirements warrant continuation of the assessments.

As of December 1, 2009, members prepaid discounted assessments totaling $85.7 million. In 2009, one fifth of the total undiscounted amount of the prepaid assessments was recorded as contribution to capital. The remaining portion of the prepaid assessments was recorded as deferred premium assessments. The prepayment discount is being amortized at annual rate of 7% and amortization of $.5 million was recorded as an offset to investment income in 2009. As of December 31, 2009, a deficient premium receivable was recorded for the portion of the first installment of the deficient premium assessment that was not prepaid.

Deficiency Assessments

The deficiency assessments are prospective in nature, and will be determined on a year-to-year basis over the next five years (2010-2014). The exposure base for these deficiency assessments will be calculated in accordance with the policy year accumulated standard earned premium at Designated Statistical Reporting ("DSR") level methodology as defined by the Minnesota Workers' Compensation Insurers Association. For each year of the deficiency assessments, self-insurers and policyholders will pay deficiency assessments based on their estimated DSR premium for the year, subject to subsequent true-up audit adjustments. Deficiency assessments will be recorded as a contribution to capital on an annual basis beginning in 2010.

10. Contingencies

During 2008, the Association reached a $20 million settlement of a lawsuit against American International Group ("AIG") charging that AIG had understated its workers' compensation premiums in Minnesota since 1985. The settlement compensated the Association for unpaid reinsurance premiums and lost investment income. The Association received $16.5 million in cash and recorded a $3.5 million receivable for offsets against future claims payable to AIG.

In October 2008, the Association, along with three other Minnesota nonprofit organizations, filed a lawsuit against Wells Fargo Bank, N.A., in Minnesota District Court in Ramsey County. The lawsuit relates to the Wells Fargo securities lending program and charges that Wells Fargo breached contracts, breached fiduciary responsibilities, and engaged in misrepresentations and other wrongful conduct in connection with the program. The lawsuit seeks to recover significant losses incurred by the Association from participation in the Wells Fargo securities lending program. The trial has been scheduled for April 19, 2010.

Workers' Compensation Reinsurance Association®

Offices
Suite 1700
400 Robert Street North
Saint Paul, MN 55101-2026

Phone 651-293-0999 or 800-293-8006

Fax 651-229-1848

Email wcra@wcra.biz

Website www.wcra.biz