McGladrey & Pullen
Certified Public Accountants

North Carolina Insurance Underwriting Association

Financial Report
(Statutory Basis)
09.30.2008

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McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report

To the Board of Directors
North Carolina Insurance Underwriting Association
Cary, North Carolina

We have audited the accompanying statutory statements of admitted assets, liabilities and members' surplus of North Carolina Insurance Underwriting Association (the "Association") as of September 30, 2008 and 2007, and the related statutory statements of operations and changes in members' surplus, and cash flows for the years then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 financial statements, the Association prepared these financial statements using accounting practices prescribed or permitted by the Insurance Department of the State of North Carolina, which practices differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between the statutory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Association as of September 30, 2008 and 2007, or the results of its operations or its cash flows for the years then ended.

The Association did not obtain an updated actuarial valuation as of and for the year ended September 30, 2008 for its postretirement health and life insurance benefits. Therefore, these financial statements do not include certain disclosures relating to the postretirement health and life insurance benefits that are derived from actuarial studies. In our opinion, disclosure of this information is required by statutory accounting practices.

The Association did not prepare the supplementary information required by accounting practices prescribed or permitted by the Insurance Department of the State of North Carolina. Therefore, these financial statements do not include those disclosures. In our opinion, disclosure of this information is required by statutory accounting practices.

In our opinion, except for the omission of the information discussed in the preceding two paragraphs, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and members' surplus of the Association as of September 30, 2008 and 2007, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in Note 1.

As described in Note 2 to the financial statements, the Association's loss exposure has increased very rapidly in recent years due to several factors. A very severe hurricane could produce losses that would require the Association to assess the member companies' amounts totaling several billion dollars. The ability of the Association to pay claims to insureds from such a storm and the timing of those payments depend upon receipts of those assessments from the member companies. During the year ended September 30, 2008, the North Carolina General Assembly formed a commission to provide recommendations to address this situation.

McGladrey & Pullen, LLP

Greensboro, North Carolina
April 6, 2009

North Carolina Insurance Underwriting Association

Statutory Statements of Admitted Assets, Liabilities, and Members' Surplus
September 30, 2008 and 2007

	2008	2007
Admitted Assets		
Cash and short-term investments	$ 254,401,039	$ 326,760,455
Bonds and other debt instruments (Note 3)	444,019,350	200,831,204
Cash and invested assets	698,420,389	527,591,659
Interest income due and accrued	3,665,683	2,316,691
Other receivables, net	470,013	517,113
Data processing equipment, at cost less accumulated depreciation of $515,150 in 2008 and $600,695 in 2007	110,087	133,162
Total admitted assets	$ 702,666,172	$ 530,558,625
Liabilities and Members' Surplus		
Liabilities:		
Unpaid losses (Notes 2 and 4)	$ 7,602,893	$ 5,990,717
Unpaid loss adjustment expenses (Notes 2 and 4)	515,638	471,068
Unearned premiums	149,304,076	126,642,268
Remittances and items not allocated	9,273,163	7,641,411
Net due to North Carolina Joint Underwriting Association (Note 5)	287,029	1,239,882
Accounts payable and accrued expenses (Note 8)	5,474,623	3,531,388
Distributions payable	-	40,134
Total liabilities	172,457,422	145,556,868
Commitments and contingencies (Notes 2, 6 and 7)		
Members' surplus	530,208,750	385,001,757
Total liabilities and members' surplus	$ 702,666,172	$ 530,558,625

See Notes to Statutory Financial Statements.

North Carolina Insurance Underwriting Association

Statutory Statements of Operations and Changes in Members' Surplus
Years Ended September 30, 2008 and 2007

	2008	2007
Direct premiums written	**277,956,547**	$ 226,852,936
Change in unearned premiums	**(22,661,808)**	(31,830,690)
Ceded reinsurance premiums	**(78,097,116)**	(32,827,454)
	177,197,623	162,194,792
Underwriting expenses (Notes 4, 6 and 9):		
Losses incurred	**11,154,608**	9,757,690
Loss adjustment expenses incurred	**1,037,632**	1,082,884
Commissions	**35,870,188**	29,230,823
Salaries and benefits	**2,071,095**	2,155,624
Insurance taxes, licenses and fees	**7,433,702**	5,007,226
Occupancy	**218,061**	289,972
Postage	**299,490**	262,493
Credit card service fees	**357,693**	234,215
Information technology	**109,232**	89,417
Depreciation	**132,656**	119,558
Other	**224,173**	67,098
Total underwriting deductions	**58,908,530**	48,297,000
Net underwriting gain	**118,289,093**	113,897,792
Investment income:		
Interest income	**26,828,634**	21,464,747
Net income	**145,117,727**	135,362,539
Members' surplus:		
Beginning	**385,001,757**	249,982,407
Distributions to members (Note 8)	**(14,968,232)**	(6,463,139)
Assessments of members (Note 8)	**14,968,232**	6,463,139
Change in nonadmitted assets	**89,266**	(343,189)
Ending	**$ 530,208,750**	$ 385,001,757

See Notes to Statutory Financial Statements.

North Carolina Insurance Underwriting Association

Statutory Statements of Cash Flows
Years Ended September 30, 2008 and 2007

	2008	2007
Cash Flows From Operations		
Premiums collected net of reinsurance	**$ 201,538,283**	$ 195,525,737
Losses and loss adjustment expenses paid	**(10,535,494)**	(17,031,064)
Net interest income	**25,479,642**	20,986,692
Underwriting expenses paid	**(45,613,567)**	(37,732,106)
Net cash from operations	**170,868,864**	161,749,259
Cash Flows From Investments		
Cost of long-term investments acquired:		
Bonds and other debt instruments	**(364,198,519)**	(88,087,073)
Proceeds from investments sold, matured or repaid:		
Bonds and other debt instruments	**121,010,373**	39,628,418
Net cash from investments	**(243,188,146)**	(48,458,655)
Cash Flows From Financing and Miscellaneous Sources		
Assessments	**14,968,232**	6,463,139
Distributions	**(15,008,366)**	(7,300,853)
Net cash from financing and miscellaneous sources	**(40,134)**	(837,714)
Net increase (decrease) in cash and short-term investments	**(72,359,416)**	112,452,890
Cash and short-term investments:		
Beginning	**326,760,455**	214,307,565
Ending	**$ 254,401,039**	$ 326,760,455

See Notes to Statutory Financial Statements.

Note 1. Nature of Organization and Significant Accounting Policies

North Carolina Insurance Underwriting Association (the "Association") was formed August 15, 1969 as a mandatory association of insurance companies ("Members") authorized to write fire, extended coverage and vandalism and malicious mischief coverage in the State of North Carolina. The purpose of the Association is to assist applicants in securing adequate property insurance in the coastal areas of North Carolina when not obtainable in the customary insurance market. The majority of the Association's policies are submitted by independent producers, who remit premiums directly to the Association. In recent years the number of policies issued has increased substantially.

The Association is administered by a Board of Directors elected by the Members and is subject to the supervision of the Commissioner of Insurance of the State of North Carolina. The manager of the Association is appointed by the Board of Directors.

For the year ended September 30, 2008, the Association had members' surplus of $530,208,750. By statute, the Association has the ability to assess Member companies for all losses.

A summary of the Association's significant accounting policies is as follows:

Basis of presentation: At the direction of the Commissioner of Insurance of the State of North Carolina, the Association presents its financial statements on the basis of accounting practices prescribed or permitted by the North Carolina Department of Insurance. The State of North Carolina has adopted the National Association of Insurance Commissioners' ("NAIC") statutory accounting practices ("SAP") as the basis of its statutory accounting practices.

In addition, the Commissioner of the North Carolina Department of Insurance has the right to permit other specific practices that may deviate from prescribed practices.

Accounting practices and procedures of the NAIC as prescribed or permitted by the insurance department of the applicable state of domicile comprise a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America ("GAAP"). The more significant differences are as follows:

Investments in bonds and other debt instruments are generally reported at amortized cost, unless required to be reported at market value by NAIC regulations. Under GAAP, investments in debt securities are designated at purchase as held-to-maturity, trading securities, or available-for-sale. Held to maturity debt securities are reported at amortized cost, less applicable valuation allowances, and other debt securities are report at fair value under GAAP. For debt securities designated as trading, unrealized holding gains and losses are reported in operations and for those designated as available-for-sale, unrealized holding gains and losses are reported as a separate component of equity, under GAAP.

Commissions, premium taxes and other costs relating to the acquisition, issuance and renewal of policies are charged to operations as incurred, rather than being deferred and amortized over the term of the policy.

Certain assets, described as nonadmitted, are excluded from the balance sheet by direct charges to surplus. In accordance with GAAP, such assets are recorded on the balance sheet, net of valuation allowances.

Note 1. Nature of Organization and Significant Accounting Policies (Continued)

The defined benefit pension and postretirement obligations are determined excluding nonvested employees. In accordance with GAAP, nonvested employees are included in the valuations.

If the accumulated benefit obligation exceeds the fair value of the defined benefit pension plan's assets, a minimum pension liability is required and recorded through net income (loss) in the current year under SAP. Under GAAP, the funded status (plan assets less than benefit obligations) of the Plan is recognized on the balance sheet as an asset or liability with a corresponding charge or credit to accumulated other comprehensive income.

Assets and liabilities related to insurance and reinsurance activities are netted in financial statements prepared on the basis of SAP. Under GAAP, those assets and liabilities would be reported at their gross amounts.

The statements of cash flows are prepared and presented in accordance with guidelines established by the NAIC rather than those established by Financial Accounting Standards Board Statement No. 95, *Statement of Cash Flows.*

Cash and short-term investments: Cash constitutes a medium of exchange that a bank will accept for deposit and allow an immediate credit to the depositor's account. Also classified as cash for financial statement purposes, although not falling within the above description of cash, are cash equivalents which include savings accounts and certificates of deposit in banks and other similar institutions with maturity dates of one year or less from the acquisition. At times cash deposits with a financial institution may exceed federally insured limits. The Association has not experienced any credit losses related to such deposits and its management is not aware of any events or circumstances which would raise doubt about the ongoing solvency of the institution.

Investments with remaining maturities of one year or less at the time of acquisition (excluding those investments defined as cash equivalents above) are considered short-term investments. From time to time the Association holds investments in money market instruments that are reported in accordance with the guidance in the NAIC *Purposes and Procedures of the Securities Valuation Office ("SVO"),* which is generally the reported net asset value.

Investments: Bonds are reported at amortized cost in the accompanying statutory financial statements. Prepayment assumptions for asset-backed securities were obtained from broker dealer survey values or internal estimates. Realized gains and losses on sales of investments are recognized in the statutory statements of operations on a specific-identification basis. Declines in fair value that are considered other-than-temporary are charged to realized losses and the cost of the investment is adjusted to estimated fair value in the period when the determination is made. In determining whether these losses are expected to be temporary, the Association considers severity of impairment, duration of impairment, forecasted market price recovery, and the intent and ability of the Association to hold the investment until the market price has recovered.

Accrued investment income: The Association nonadmits investment income due and accrued if amounts are over 90 days past due. As of September 30, 2008 and 2007, the Association had no income due or accrued over 90 days past due.

Note 1. Nature of Organization and Significant Accounting Policies (Continued)

Premiums in course of collection: The Association records premiums in course of collection at total unpaid balance, which approximates estimated fair value, net of any nonadmitted receivables. The Association determines past due status of individual accounts receivable based on the effective date of the policy and generally does not charge interest on past due amounts. Premiums that management believes to be ultimately not collectible are written off upon such determination. Any premiums considered to be past due 90 days or more are nonadmitted.

Fixed assets: Fixed assets are carried at cost less accumulated depreciation. The Association provides for depreciation on admitted assets using the straight-line method over three to five years. Depreciation expense was $132,656 and $119,558 for the years ended September 30, 2008 and 2007, respectively. Maintenance and repairs are charged to expense as incurred.

Nonadmitted assets: Certain assets designated as nonadmitted assets have been charged directly to members' surplus. Amounts related to nonadmitted assets are as follows:

	2008	2007
Furniture and equipment, less accumulated depreciation of $443,716 in 2008 and $235,799 in 2007	**$ 330,731**	$ 197,766
Prepaid expenses	**90,752**	51,969
Accounts receivable, assessments	**168,015**	429,029
	$ 589,498	$ 678,764

Depreciation on nonadmitted assets (furniture and equipment) is computed by applying the straight-line method over the estimated useful lives of the related assets. Estimated lives are three to five years for furniture and equipment. This depreciation expense is reflected in the statements of operations with a corresponding credit to members' surplus.

Reserves for losses and loss adjustment expenses: Unpaid losses and loss adjustment expenses include an amount determined from individual case estimates and loss reports and an amount, based on past experience, for losses incurred but not reported. Such liabilities are necessarily based on assumptions and estimates and, while management believes the amount is adequate, the ultimate liability may be in excess of or less than the amount provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed and any adjustments are reflected in the period determined.

Establishing liabilities for claims is subject to significant uncertainties that make reserve estimation difficult. Legal decisions have tended to expand insurance coverage beyond the intent of the original policies. The disposition of such requires lengthy and costly litigation. In establishing liabilities for claims, the Association considers all pertinent information as it becomes available and establishes incurred but not reported reserves where appropriate. Although the reserves are deemed adequate to cover all probable claims, there is a reasonable possibility that adverse development from prior accident years could occur in the future.

Note 1. Nature of Organization and Significant Accounting Policies (Continued)

Estimates for catastrophic events are inherently more uncertain than those for non-catastrophic losses due to the unique circumstances involving a catastrophe. Due to the low frequency of historical catastrophic events, standard actuarial loss development methods are difficult to apply and may result in a wider range of estimates of ultimate catastrophic losses. Therefore, material changes to estimates related to these events are reasonably possible in the near term after these events occur and are reflected in operations as more information becomes available.

Reinsurance: Reinsurance premiums and liabilities related to reinsurance ceded are accounted for on a basis consistent with that used in accounting for the original policies issued by the Association and the terms of the reinsurance contract. Premiums and losses on reinsurance ceded are reported as reductions of premiums earned and losses and loss adjustment expenses incurred, respectively, in the statutory statements of operations and changes in members' surplus.

Member participation: Each member's participation in the operations of any fiscal year is in proportion to that member's North Carolina insurance writings for the affected lines of business in the preceding calendar year. Participation percentages vary from year to year. Assessments of members related to each fiscal year are based on their participation. Since the Association has the authority to assess its members to cover members' deficits, members can be assessed annually to meet the liquidity requirements of the Association. Special assessments are also permitted for large unanticipated losses.

Premiums and related commissions: Premiums are earned over the periods covered by the policies on a pro-rata basis. Unearned premium reserves are established to cover the unexpired portion of premiums written. Expenses incurred related to the acquisition of new insurance business, including such acquisition costs as commissions, premium taxes and other underwriting expenses, are charged to expense when incurred.

Income taxes: The Association has received correspondence from the Internal Revenue Service indicating that it is tax-exempt under Section 501(c)(6) of the Internal Revenue Code.

Use of estimates: The preparation of financial statements in accordance with SAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ significantly from those estimates.

Note 2. Significant Increased Exposure to Coastal Properties

As many insurers have lessened their voluntary writings of policies covering North Carolina coastal properties over the past few years, and as pricing of policies has become much less competitive for coverages in coastal areas, the Association has seen an unprecedented increase in exposure. Amplifying this exposure is the fact that during this period of time market prices for coastal properties have also substantially increased. The Association currently has approximately $72 billion of exposure along the North Carolina coast.

Management estimates indicate that a very severe hurricane could produce losses that would require the Association to assess the member companies' amounts totaling several billion dollars. The ability of the Association to pay claims to insureds from such a storm and the timing of those payments depend upon receipts of those assessments from the member companies. There is an increased concern that a major storm could result in assessments which may threaten the existence of some smaller insurers.

Note 2. Significant Increased Exposure to Coastal Properties (Continued)

During the year ended September 30, 2008, the North Carolina General Assembly formed a commission to provide recommendations to address this situation. The commission made recommendations to the 2009 Session of the North Carolina General Assembly that included, among other things, adjustments to Association premiums and deductibles, reduction of maximum property coverages, adjustments to the methods of making assessments against insurers, and consideration of damage mitigation measures and how they should be taken into account. It is uncertain what measures, if any, the 2009 Session of the North Carolina General Assembly may enact to address the current situation.

Note 3. Bonds and Other Debt Instruments

Since most of the Association's investments consist of securities that are traded in the public securities markets, they are subject to risk related to fluctuations in overall market performance and are potentially subject to heightened levels of market risk attributable to issuer, industry, and geographic region concentrations. Investments in debt securities subject an investor to credit risk, and concentrations in debt securities of single issuers, issuers operating in similar industries, or securities backed by similar collateralizing assets subject an investor to heightened levels of credit risk. The Company's investment portfolio is regularly reviewed and the extent of its diversification is considered in the context of statutory requirements and other risk management and performance objectives.

Amortized cost (admitted amount), aggregate market value and gross unrealized gains and losses pertaining to the portfolio of bonds and other debt instruments as of September 30, 2008 and 2007 are as follows:

	September 30, 2008			
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized (Losses)**	**Market Value**
U. S. Treasury obligations	$ 41,057,973	$ -	$ (368,773)	$ 40,689,200
Federal agency obligations	402,961,377	1,568,926	(3,106,238)	401,424,065
	$ 444,019,350	$ 1,568,926	$ (3,475,011)	$ 442,113,265

	September 30, 2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Market Value
Federal agency obligations	$ 200,831,204	$ 1,209,241	$ (442,594)	$ 201,597,851

Debt securities, other than short-term investments of $63 million, are all included in bonds and other debt instruments in the accompanying statutory statement of admitted assets, liabilities and members' surplus as of September 30, 2008. Debt securities, other than short-term investments of $158 million, are all included in bonds and other debt instruments in the accompanying statutory statement of admitted assets, liabilities and members' surplus as of September 30, 2007. The estimated fair value of bonds and other debt instruments as of September 30, 2008 and 2007, excluding any short-term investments, approximated NAIC market values since substantially all issues owned by the Association are public issues for which quoted prices are available.

Note 3. Bonds and Other Debt Instruments (Continued)

Amortized cost and aggregate market value of bonds and other debt instruments held as of September 30, 2008, according to final contractual maturity dates, are as indicated below. Actual future maturities will differ from the maturities shown because certain issuers have the right to call or prepay obligations.

	Amortized Cost	Market Value
Amounts due in less than one year	$ 19,887,342	$ 20,103,100
Amounts due after one year through five years	169,482,752	169,881,203
Amounts due after five years through ten years	118,544,763	117,653,150
Amounts due after ten years through twenty years	136,104,493	134,475,812
	$ 444,019,350	$ 442,113,265

There were no significant sales of bonds and other debt instruments during the years ended September 30, 2008 or 2007.

The following table shows unrealized gross losses and fair value, for the Association's investments, aggregated by individual category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2008:

	12 Months or Less		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U. S. Treasury obligations	$ 40,689,200	$ 368,773	$ -	$ -	$ 40,689,200	$ 368,773
Federal agency obligations	224,631,187	2,473,983	48,910,042	632,255	273,541,229	3,106,238
	$ 265,320,387	$ 2,842,756	$ 48,910,042	$ 632,255	$ 314,230,429	$ 3,475,011

The following table shows unrealized gross losses and fair value, for the Association's investments, aggregated by individual category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2007:

	12 Months or Less		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Federal agency obligations	$ 47,742,522	$ 354,846	$ 35,583,607	$ 87,748	$ 83,326,129	$ 442,594

Note 3. Bonds and Other Debt Instruments (Continued)

The temporary impairments in the tables above were caused by market conditions. The Association relies on its investment manager's guidance to address such factors as industry analyst reports, sector credit ratings, volatility of a particular security's market price, and/or any other information that the Association may need to take into consideration in determining if other than temporary impairments exist. Based on past experience and current knowledge, the Association believes that investment managers typically do not hold investments for which there is little chance of appreciation during the short term, and therefore none of the above investments constitutes a situation which would require an adjustment of cost basis of the investment for an impairment.

Investment income, net of investment expenses, which are not material, for the years ended September 30, 2008 and 2007 is comprised of primarily interest on bonds and other debt instruments and short-term investments.

Subsequent to year-end, the credit and liquidity crisis in the United States and throughout the global financial system has resulted in substantial volatility in financial markets and the banking system. These and other economic events have had a significant adverse effect on investment portfolios. As a result, the Association's investments may have incurred a significant decline in fair value since September 30, 2008.

Note 4. Reserve for Losses and Loss Adjustment Expenses

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

	2008	2007
Balance at October 1	**$ 6,461,785**	$ 12,652,275
Incurred related to:		
Current year	**12,207,821**	14,872,789
Prior years	**(15,581)**	(4,032,215)
Total incurred	**12,192,240**	10,840,574
Paid related to:		
Current year	**(5,689,494)**	(10,150,545)
Prior years	**(4,846,000)**	(6,880,519)
Total paid	**(10,535,494)**	(17,031,064)
Balance at September 30	**$ 8,118,531**	$ 6,461,785

As a result of changes in estimates related to insured events of prior years, the provision for losses and loss adjustment expenses was adjusted as indicated in the table above. The decrease in prior year incurred losses and loss adjustment expenses in 2008 and 2007 resulted from favorable development of claims on an overall basis. No individual events were responsible for a large change in prior year incurred claims.

Note 4. Reserve for Losses and Loss Adjustment Expenses (Continued)

The components of unpaid losses and loss adjustment expenses as of September 30, 2008 and 2007 are as follows:

	2008	2007
Unpaid losses:		
Case basis	$ 2,917,957	$ 1,961,935
Incurred but not reported	4,684,936	4,028,782
	$ 7,602,893	$ 5,990,717
Unpaid loss adjustment expenses:		
Case basis	$ 225,515	$ 173,679
Incurred but not reported	290,123	297,389
	$ 515,638	$ 471,068
	$ 8,118,531	$ 6,461,785

Note 5. Related Party Transactions

A related organization, North Carolina Joint Underwriting Association ("NCJUA"), shares the same facility and is operated by the same personnel as the Association. This arrangement periodically results in receivables or payables between the two associations. At September 30, 2008, the Association had a net payable to NCJUA of $287,029. At September 30, 2007, the Association had a net payable to NCJUA of $1,239,882.

Note 6. Lease Commitments

The Association and NCJUA jointly rent home office facilities under an operating lease agreement, which expires in 2015. The Association is currently allocated 62% of the costs under this lease agreement. The Association's allocated share of rent expense was $218,061 in 2008 and $289,972 in 2007.

The Association's share of the rent commitments, based on current cost sharing provisions with NCJUA, under the terms of operating lease agreements at September 30, 2008 is as follows:

Year Ending September 30,	Amount
2009	$ 324,626
2010	324,601
2011	313,358
2012	298,303
2013	297,372
Thereafter	356,323
	$ 1,914,583

The Association is also required to pay a proportionate share of operating expense increases during the lease term for the building.

Note 7. Litigation

In the ordinary course of business, the Association from time to time is involved in lawsuits filed under various causes of action. In the opinion of management, ultimate disposition of these actions will not have a material effect on the Association's financial condition.

Note 8. Assessments of and Distributions to Members

Under North Carolina law, the Association may make assessments of its members and may also make periodic distributions to its members.

An assessment and an offsetting distribution totaling $14,968,232 was made in 2008. An assessment and an offsetting distribution totaling $6,463,139 was made in 2007.

Note 9. Employee Benefit Plans

The Association and NCJUA are members of a multiple-employer pension trust. Employees who are hired before age 60 and who are scheduled to work 1,000 hours in a 12-month period are eligible for the plan upon their date of hire. No employee contributions are required. The Association's funding policy is to make the minimum annual contributions required by applicable regulations, which are based on recommendations from the plan's actuary. The Association is currently allocated 62% of the costs and obligations associated with their participation in the plan under the current cost-sharing arrangement with NCJUA.

In addition to pension benefits, the Association and NCJUA provide certain health care and life insurance ("postretirement") benefits for retired employees. The costs and accrued liabilities associated with these benefits are allocated between the two entities in the same proportions as for the pension plan. Retirees are eligible to continue medical coverage on a contributory basis and will continue to receive the same basic life insurance until age 65 at which time the coverage will be reduced to $5,000. Current employees and part-time employees who work at least 20 hours per week can become eligible for these life insurance benefits by retiring after meeting the age and service requirements of age 55 and 15 years of service. Medical benefit eligibility requirements are age 50 with 65 points (age plus service) or age 65 with 5 years of service. Spouses and dependent children of these retirees are also eligible to participate.

The Association uses a September 30 measurement date for its plans.

Note 9. Employee Benefit Plans (Continued)

Obligations and Funded Status

	Pension Benefits	
	2008	2007
Changes in benefit obligations:		
Obligations at beginning of year	**$ 1,954,717**	$ 1,066,761
Service cost	**135,440**	128,036
Interest cost	**122,732**	100,433
Participant contributions	**-**	-
Actuarial (gains) losses	**(304,073)**	153,186
Benefits paid	**(66,719)**	(80,418)
Change in cost sharing with NCJUA	**-**	586,719
Obligations at end of year	**1,842,097**	1,954,717
Changes in plan assets:		
Fair value of assets at beginning of year, primarily pooled separate accounts with insurance companies and mutual funds	**1,544,679**	897,261
Actual return on assets	**(246,213)**	123,816
Association contributions	**124,528**	110,525
Participant contributions	**-**	-
Benefits paid	**(66,719)**	(80,418)
Change in cost sharing with NCJUA	**-**	493,495
Fair value of assets at end of year, primarily pooled separate accounts with insurance companies and mutual funds	**1,356,275**	1,544,679
Funded status (plan assets less than benefit obligations) at end of years	**(485,822)**	(410,038)
Amounts not recognized on statutory statements of admitted assets, liabilities, and members' surplus:		
Unrecognized net loss	**354,552**	296,447
Net amount recognized on statutory statements of admitted assets, liabilities, and members' surplus	**(131,270)**	(113,591)

Note 9. Employee Benefit Plans (Continued)

	Pension Benefits	
	2008	2007
Amounts recognized on statutory statements of admitted assets, liabilities, and members' surplus as:		
Accrued benefit cost	**$ (131,270)**	$ (113,591)
Additional minimum liability	**-**	-
Net amount recognized on statutory statements of admitted assets, liabilities, and members' surplus	**(131,270)**	(113,591)
Aggregate accumulated benefit obligation for defined benefit pension plan	**1,604,364**	1,684,258
For pension plan with accumulated benefit obligation in excess of assets at September 30 of the respective years:		
Projected benefit obligation	**1,842,097**	1,954,717
Accumulated benefit obligation	**1,604,364**	1,684,258
Fair value of plan assets	**1,356,275**	1,544,679

Components of Net Periodic Benefit Cost and Additional Information

	Pension Benefits	
	2008	2007
Components of net periodic benefit cost:		
Service cost	**$ 135,440**	$ 128,036
Interest cost	**122,732**	100,433
Recognized actuarial loss	**8,940**	-
Expected return on plan assets	**(124,906)**	(112,823)
Net periodic benefit cost	**142,206**	115,646
Additional information:		
Increase (decrease) in minimum liability included in net income	**-**	-

Assumptions

	Pension Benefits	
	2008	2007
Weighted-average assumptions used in computing ending obligations:		
Discount rate	**7.25%**	6.00%
Rate of compensation increase	**4.00**	4.00
Weighted-average assumptions used in computing net cost:		
Discount rate	**6.00**	5.75
Rate of compensation increase	**4.00**	4.00
Expected return on net assets	**8.00**	8.00

Note 9. Employee Benefit Plans (Continued)

The expected rate of return on plan assets was determined based on the average rate of earnings expected to be earned on the current and target asset categories.

For measurement purposes, the discount rate used in 2007, when the Association last obtained an actuarial valuation of its postretirement health and life insurance benefits, in determining the accumulated postretirement benefit obligation was 6.0%, and the health care cost-trend rate was 9.0% decreasing 0.5% per year to an ultimate rate of 5.0% in 2015. A nonvested accumulated postretirement benefit obligation of $924,082 existed at September 30, 2007.

A nonvested pension projected benefit obligation and accumulated benefit obligation of $98,378 and $89,684, respectively, existed at September 30, 2008. A nonvested pension projected benefit obligation and accumulated benefit obligation of $132,382 existed at September 30, 2007.

The Medicare Prescription Drug Improvement and Modernization Act of 2003 was enacted during 2003 (the "Act"). The Act creates Medicare Part D which could have some effect on the Association's obligations under the postretirement health plan. Measures of the accumulated postretirement benefit obligation and the net periodic benefit cost recorded in these financial statements do not reflect any changes brought about by the Act because the employer is unable to conclude whether the benefits provided by the plan are actuarially equivalent to Medicare Part D under the Act.

Plan Assets

The Association participates in a multiple employer pension plan called the Insurance Organizations Employees' Retirement Plan (the "Plan"). Plan assets are held in a single trust for all employers who participate in the Plan. Each year, assets are allocated to the Association based on its historical contributions, benefit disbursements, and share of investment return.

The asset allocation for the Plan at the end of the Association's fiscal year, and the ongoing target allocation, by asset category, follows:

Asset Category	Target	As of September 30, 2008	As of September 30, 2007
Equity securities	75 %	70 %	74 %
Debt securities	25	26	22
Cash	-	4	4
Total	100 %	100 %	100 %

The Plan's investment policy is set by the Trustees of the Insurance Organization Pension Trust. Plan assets are invested to generate a long-term investment return (net of management and administrative fees) that exceeds the Consumer Price Index ("CPI") inflation rate by at least 5.0%. Long-term investment results are measured over rolling periods of eight to ten years.

Note 9. Employee Benefit Plans (Continued)

Cash Flows

The Association expects to contribute approximately $150,000 to its pension plan and approximately $22,000 to its other postretirement benefit plan in fiscal year 2009.

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

Year	Pension Plan
2009	$ 90,443
2010	97,839
2011	104,915
2012	111,115
2013	115,753
2014 - 2018	700,862

Defined Contribution Plan

The Association also offers an Employee Savings Plan to employees working at least 1,000 hours in a year. This plan is offered through a multiple-employer arrangement with the Association matching 75% of employee contributions up to 6% of the employee's earnings. The Association's expense for the years ended September 30, 2008 and 2007 was $70,349 and $63,179, respectively.

Note 10. Estimated Fair Values of Financial Instruments

Due to their short-term maturity or settlement, the fair values of cash and short-term investments, balances due on account from insureds and others, payables, and remittances and items not allocated approximate their carrying amounts as reflected in the statutory statements of admitted assets, liabilities and members' surplus. The fair value and amortized cost of bonds and other debt instruments are estimated based on quoted market prices and approximated $442,113,000 and $444,019,000, respectively, at September 30, 2008. The fair value and amortized cost of bonds and other debt instruments approximated $201,598,000 and $200,831,000, respectively, at September 30, 2007.

The Association has not historically maintained financial instruments for trading purposes.

Note 11. Reinsurance Agreement

The Association, along with the North Carolina Joint Underwriting Association (collectively, the "Associations"), has entered into joint property catastrophe excess of loss reinsurance agreements on a per risk basis covering risks located in the beach and coastal counties of North Carolina, as defined by the Association, in order to reduce its exposure to wind losses that may result from a catastrophic event. For 2008, in the event of a named storm, the Associations retain the first $1.1 billion of loss, 20% of loss in the layer $0.3 billion excess of $1.1 billion, 27.1571% of loss in the layer $0.5 billion excess of $1.4 billion, 20.8268% of loss in the layer $0.5 billion excess of $1.9 billion, and all loss above $2.4 billion. The agreement does allow for reinstatement in the case of a loss event. In the case of a reinstatement, the Associations would be required to pay additional premiums for the reinstated coverage. The reinsurers' responsibility for losses from all loss occurrences during the term of the contract cannot exceed $2.6 billion. The 2008 reinsurance agreement covers the period from May 1, 2008 to May 1, 2009. The Association also purchased a joint property catastrophe excess of loss reinsurance agreement on a per risk basis during 2007 that coved the period May 1, 2007 to May 1, 2008.

Information about reimbursed losses and loss adjustment expenses related to the above agreement for the year ended September 30, 2008 follows:

Reinsurance recoverable on losses and loss adjustment expense as of September 30	$ -
Reinsurance recoverable on unpaid losses and loss adjustment expenses as of September 30	-
Reinsurance recoveries on incurred claims during the year	-

For this catastrophe coverage the Associations are charged a provisional premium, which may be adjusted in accordance with a formula included in the reinsurance agreement for each excess layer if the limits of insurance in force increase or decrease by an average of greater than 10%. The effect of reinsurance on premiums written and earned during the years ended September 30, 2008 and 2007 is as follows:

	2008		2007	
	Written	**Earned**	Written	Earned
Direct	**$ 277,956,547**	**$ 255,294,739**	$ 226,852,936	$ 195,022,246
Ceded	**(78,097,116)**	**(78,097,116)**	(32,827,454)	(32,827,454)
Net premiums	**$ 199,859,431**	**$ 177,197,623**	$ 194,025,482	$ 162,194,792

The reinsurance contract does not relieve the Associations of their primary obligation to policyholders and failure of the reinsurers to discharge their obligations could result in losses to the Associations. The Associations regularly evaluate the financial condition of their reinsurers and monitor concentrations of credit risk related to their reinsurance activities. No credit losses resulted from ceded reinsurance activities during the years ended September 30, 2008 or 2007.

There is no unsecured reinsurance recoverable on paid and unpaid losses and loss adjustment expenses for individual reinsurers whose balances exceeded 3% of the Association's surplus as of September 30, 2008 or 2007.

The maximum amount of return commission which would have been due reinsurers if either the reinsurers or the Association had canceled the Association's reinsurance as of the end of the year ended September 30, 2008 or 2007 is not material.