

Meeting New Challenges: Insuring the Future of Public Housing



1999 ANNUAL REPORT

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Housing Authority Insurance Membership 1999

Anniston, AL	Breckenridge, CO	Homestead, FL	La Grange, GA	Fort Wayne, IN	Fitchburg, MA
Auburn, AL	Denver, CO	Key West, FL	Lavonia, GA	Gary, IN	Gloucester, MA
Birmingham, AL	Limon, CO	Lakeland, FL	Louisville, GA	Hammond, IN	Groveland, MA
Decatur, AL	Pueblo, CO	Lauderhill, FL	Macon, GA	Indianapolis, IN	Hanson, MA
Jacksonville, AL	Ansonia, CT	Miami, FL	Madison, GA	Jeffersonville, IN	Haverhill, MA
Lafayette, AL	Bridgeport, CT	Monroe County, FL	Manchester, GA	Kendallville, IN	Holyoke, MA
Mobile, AL	Bristol, CT	Orlando, FL	Marietta, GA	Kokomo, IN	Hudson, MA
Montgomery, AL	Cheshire, CT	Palm Beach County, FL	Metter, GA	Michigan City, IN	Lawrence, MA
Ozark, AL	Danbury, CT	FL	Millen, GA	Mishawaka, IN	Lowell, MA
Amity, AR	East Hartford, CT	Panama City, FL	Monroe, GA	Muncie, IN	Malden, MA
Arkadelphia, AR	Glastonbury, CT	Pensacola, FL	Mount Vernon, GA	Richmond, IN	Marlborough, MA
Camden, AR	Greenwich, CT	Plant City, FL	Norcross, GA	South Bend, IN	Melrose, MA
Dardanelle, AR	Hamden, CT	Sarasota, FL	Palmetto, GA	Atchison, KS	Methuen, MA
Little Rock, AR	Hartford, CT	St. Petersburg, FL	Pelham, GA	Atwood, KS	Milford, MA
Magnolia, AR	Meriden, CT	Tampa, FL	Quitman, GA	Cherryvale, KS	Milton, MA
North Little Rock, AR	Middletown, CT	Titusville, FL	Royston, GA	Colby, KS	New Bedford, MA
Ola, AR	Milford, CT	Venice, FL	Sandersville, GA	Fort Scott, KS	Newburyport, MA
Paragould, AR	Naugatuck, CT	West Palm Beach, FL	Savannah, GA	Galena, KS	Newton Highland, MA
Flagstaff, AZ	New Britain, CT	Winterhaven, FL	Screven County, GA	Goodland, KS	North Adams, MA
Nogales, AZ	New Canaan, CT	Acworth, GA	Shellman, GA	Great Bend, KS	North Andover, MA
Phoenix, AZ	New Haven, CT	Americus, GA	Swainsboro, GA	Howard, KS	North Attleboro, MA
South Tucson, AZ	New London, CT	Athens, GA	Talbot County, GA	Kansas City, KS	North Reading, MA
Tucson, AZ	Norwich, CT	Augusta, GA	Talbotton, GA	Lindsborg, KS	North Scituate, MA
Winslow, AZ	Portland, CT	Barnesville, GA	Tallapoosa, GA	Oakley, KS	Northampton, MA
Alameda, CA	Putnam, CT	Bremen, GA	Tennille, GA	Olathe, KS	Pembroke, MA
Fresno, CA	Rockville, CT	Buena Vista, GA	Thomson, GA	Parsons, KS	Pittsfield, MA
Hanford, CA	Seymour, CT	Cairo, GA	Tifton, GA	Salina, KS	Plymouth, MA
Livermore, CA	South Norwalk, CT	Carrollton, GA	Unadilla, GA	South Hutchinson, KS	Reading, MA
Lompoc, CA	Stamford, CT	Chatsworth, GA	Union City, GA	Stafford, KS	Revere, MA
Los Angeles, CA	Stratford, CT	Columbus, GA	Warrenton, GA	Topeka, KS	Rockland, MA
Madera, CA	Torrington, CT	Columbus Villas, GA	Waynesboro, GA	Wichita, KS	Saugus, MA
Martinez, CA	Wallingford, CT	Commerce, GA	Waynesboro, GA	Bowling Green, KY	Somerville, MA
Modesto, CA	Waterbury, CT	Cordele, GA	Winder, GA	Henderson, KY	Springfield, MA
Newbury Park, CA	West Hartford, CT	Crawfordville, GA	Woodbury, GA	Lexington, KY	Stow, MA
Oakland, CA	West Haven, CT	Cuthbert, GA	Woodland, GA	Lutcher, LA	Tewksbury, MA
Paso Robles, CA	Wethersfield, CT	Dalton, GA	Chicago, IL	New Orleans, LA	Vineyard Haven, MA
Port Hueneme, CA	Willimantic, CT	East Point, GA	East St. Louis, IL	Adams, MA	Wakefield, MA
Richmond, CA	Windsor Locks, CT	Ellaville, GA	North Chicago, IL	Amherst, MA	Waltham, MA
Sacramento, CA	Winsted, CT	Fairburn, GA	Peoria, IL	Andover, MA	Wayland, MA
Salinas, CA	Washington, DC	Fort Gaines, GA	Rockford, IL	Auburn, MA	Webster, MA
San Bernardino, CA	Wilmington, DE	Gainesville, GA	Anderson, IN	Belmont, MA	Woburn, MA
San Diego, CA	Clearwater, FL	Gibson, GA	Bloomfield, IN	Beverly, MA	Worcester, MA
San Francisco, CA	Crestview, FL	Greensboro, GA	Bloomington, IN	Brockton, MA	Allegany County, MD
San Jose, CA	Daytona Beach, FL	Griffin, GA	Brazil, IN	Brookline, MA	Annapolis, MD
San Luis Obispo, CA	Deerfield Beach, FL	Harlem, GA	Charlestown, IN	Cambridge, MA	Baltimore, MD
San Rafael, CA	Fort Myers, FL	Harris County, GA	Connersville, IN	Chelsea, MA	Cambridge, MD
Soledad, CA	Fort Pierce, FL	Hartwell, GA	East Chicago, IN	Chicopee, MA	Crisfield, MD
Aurora, CO	Gainesville, FL	Hogansville, GA	Elkhart, IN	Clinton, MA	Cumberland, MD
Boulder, CO	Hialeah, FL	Jackson, GA	Evansville, IN	E. Dedham, MA	
				Fall River, MA	<i>Continued on inside back cover</i>
				Falmouth, MA	

CONTINUED FINANCIAL STABILITY AND EXCEPTIONAL MEMBER SERVICE were two important achievements for Housing Authority Insurance in 1999. Losses were down, underwriting risk was reduced through reinsurance, and operational savings were realized by controlling business expenses both internally and externally.

Our level of service commitment is unmatched in the insurance industry. We retained 97% of the membership during the year, while adding 44 new members. We accomplished record service goals for member visits, risk management training, speed of underwriting service, and claim handling satisfaction. In addition, HTVN enhanced the value of the entire Housing Authority Insurance organization with more than 300 hours of training and informational broadcasting.

Our focus is on the quality of the insurance products and services we provide to the membership and our position within the market. We see the opportunity for growth ahead due to an expected "hardening" of the insurance market. Should this occur, the insurance industry will increase premiums and fewer choices will be available to housing authorities. That's when our attention to operational costs and organizational stability will pay off. Housing Authority Insurance will be there as a reliable, dependable and affordable provider of insurance products for the public housing industry. We have the systems, talent and capital to meet any growth in membership, as well as growth in the service requirements of our members.

The staff has worked hard to strengthen our relationship with our business partners and service providers to ensure continued success. We are dedicated not only to our own mission, but also to the mission of the public housing industry to provide a better life for its residents.

I recently read that "the road to success is always under construction." I think this statement holds true for Housing Authority Insurance in 1999. While it was a very successful year, we never stopped looking for ways to improve ourselves, contribute to the quality of life of public housing residents and better serve our members.



Dan Labrie
Chief Executive Officer

THIS REPORT FINDS US ENDING OUR THIRTEENTH YEAR OF OPERATION and if anything has been consistent, it is change. Not surprising since the same could easily be said of the industry we serve. CIAP to CGP to CHAS, PHMAP to PHAS, Hope VI, privatization, demolition, de-densification, Federal preferences and their demise, welfare to work, self-sufficiency...a revolving door of programs, philosophies and leadership.

As my twelfth year of involvement with Housing Authority Insurance concurrently draws to a close, I find it little short of remarkable that these companies have not only survived, but have



Barry Romano
Chairman of the Board

thrived overall, in this far less than ideal environment. We consistently look toward the horizon and evolve to meet the needs of our membership. We remain focused on our Mission and Vision Statements. We successfully rise to each new challenge, not so much from a reactive point of view, but from the more challenging and rewarding proactive perspective. Clearly a credit to the Board, staff and membership as a whole and an ongoing example that we, who are so often adversely compared to private industry, can manage very effectively when given the opportunity. I am told that many of the traditional insurers who abandoned public housing in 1987 would like to reconsider. Hopefully that will remain a lost opportunity, courtesy of our continuing focus and commitment.

At this writing, we are busily engaged in expanding our horizons as our members expand theirs. The handwriting is on the wall and it seems to say that at least the near future of public housing lies in the more entrepreneurial endeavors such as Hope VI, mixed-finance, public/private partnerships, HUD foreclosures/rehabs and other programs heralded as the departure from warehousing and isolating the poor. We are dedicated to providing for the evolving needs of our members as these initiatives come to fruition throughout the country and are again demonstrating our commitment to "...meeting new challenges and insuring the future of public housing..."

A handwritten signature in black ink, appearing to be "Barry Romano", written in a cursive style.

Meeting New Challenges: Insuring the Future of Public Housing

THERE WAS NOT ONE "BIG THING" THAT DEFINED HOUSING AUTHORITY INSURANCE IN 1999, instead it was many little things that the company — its members, Board of Directors, Committees and employees — improved upon during the year that made 1999 successful.

This attention to detail can be seen in the way we interacted with members, adjusted to difficult market conditions, focused on finances, embraced technology, and dealt with the dreaded Y2K computer problem.

Building Relationships

In 1999, Housing Authority Insurance retained 97% of its members. This exceptional retention rate can be

attributed to many activities, but among those, member contact and service stand out.

Over the course of the year, company participation in trade shows and regional housing association meetings increased 22%. Member visits made by staff totaled 231. Notably, member visits by the marketing staff increased from 81 in 1998 to 125 in 1999.

For the marketing staff, getting to know the members was a focus throughout the year. Toward this end, each marketing representative was assigned a specific geographical region in which to strengthen member relationships and build new relationships with potential members. The one-on-one contact created opportunities to discuss member needs.

The underwriting department was restructured and streamlined to create operating efficiency and improved customer service. In restructuring the department, more staff members were dedicated to customer service.

Of course, customer service doesn't end with our underwriters. For Housing Authority Insurance, it extends



The public housing industry is rebuilding itself. Demolition of old, unwelcoming structures is making way for construction of modern, comfortable homes.

Many HAI members are helping shape this change. Just look at Otłowski Gardens in Perth Amboy, NJ (pictured on the cover). Such beautiful architecture is fairly new to public housing.



The sharp contrast between these units in Galveston, TX, is indicative of the improvements occurring throughout the industry.

far beyond the essential insurance functions of providing coverage and handling claims. We provide a number of additional services that add value.

In December 1999, the company launched a new version of its Web site, www.housingcenter.com. The revamped site provides more information on our products and services, as well as more risk management and public housing articles. Customer service functionality is enhanced. Navigation is simpler. And frequent content updates are planned. The site was built and is maintained in-house.

The newsletter and a regular stream of mailings kept members informed of a variety of insurance and company-related topics. Notably, considerable effort was made in 1999 to keep members informed of Board activity. A presentation on the Board nominating process was given as part of the new member orientation session during the annual meeting. The quarterly newsletter, *Risk News*, continues to carry a regular column from the Chair, which details Board activity.

Two new programs that originated from the Board in 1999 were the PHA Scholarship Program, and the

PHA Summer Intern Program. The scholarship program provides college scholarships to residents at member authorities. The intern program provides a work experience opportunity at Housing Authority Insurance for a resident of a member authority.

Risk control education and consulting continued to be a major focus of the organization. Despite the decreased cost of risk created by the abundance of insurance options available to housing authorities, the risk management staff was able to maintain significant member participation in risk control activities.

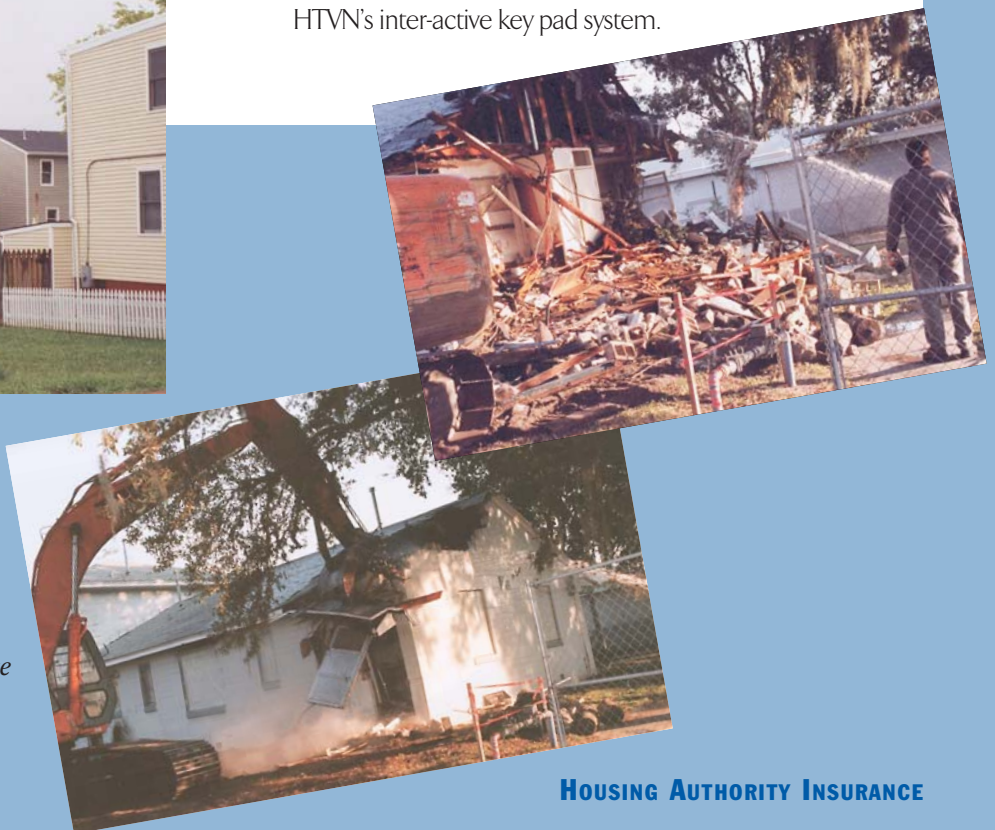
The number of regional training seminars given by the risk control staff increased from eight in 1998 to 14 in 1999. The number of participants more than doubled. There was also a sharp increase in member interest in the Fire Prevention Week Program and Poster Contest, as well as the Playground Safety Poster and Essay Contest.

Member participation in the Housing Authority Risk Retention Innovation Award program reached new heights as contest entrants made presentations to the Risk Control Committee via the Housing Television Network (HTVN). This allowed questions to be asked and answered, and voting to take place in real time using HTVN's inter-active key pad system.



These pictures tell the story of our members' success in public housing's rebuilding effort. In Richmond, VA, they've built new homes.

In St. Petersburg, FL, they tore down old concrete structures.



The risk management staff also used the HTVN interactive satellite network to provide training to members. Other services provided by the staff included one-on-one consultations, and updated risk control and law enforcement manuals.

Providing educational opportunities is important to the company. HTVN affords Housing Authority Insurance the opportunity to offer training and information to the public housing community at large. During its fourth full year of operation, HTVN broadcast more than 300 hours of programming. Many of these programs were geared toward specific career disciplines within the public housing industry as part of the National Institute of Continuing Housing Education (NICHE) certification program.

A key force of change within the industry last year was the implementation of the Housing Quality and Reform Action (QHARA). HTVN broadcast numerous programs pertinent to QHARA, including presentations on the Public Housing Assessment System, Real Estate Assessment System, and Resident Association Sub System.

Over 80 hours of HTVN programming were conducted in conjunction with the U.S. Department of Housing and Urban Development (HUD) satellite

network. Much of this programming focused on Notification of Funding Availability (NOFA). Access to these broadcasts gave HTVN members a head start in the time-sensitive NOFA process.

By the end of 1999, the HTVN network had grown from 95 to 115 member sites. More than 10,000 people participated in HTVN training sessions throughout the year. There is no comparable training and education program available to public housing authorities.

The efforts detailed above helped us achieve record-setting premiums earned, retain almost all existing members, and exceed every marketing goal for the year.

Strengthening Finances

The success of an insurance company is dictated by the strength of its finances as much as any other one factor. During 1999, Housing Authority Insurance made gains in terms of financial stability that should ensure success well into the future.

Through continual negotiations with key business partners, we were able to reduce both net loss exposure and costs related to reinsurance and fronting arrangements.



Milwaukee's Hillside Terrace was not always a very desirable place to live. These days, residents are lining up to get an apartment there.



In mid-1999, an all-lines aggregate stop loss program was completed. This program will protect the operating income and assets of the entire insurance operation. It is a major enhancement to the company's overall financial stability.

Investments, as always, received considerable attention. Both processing and performance were carefully monitored. On the processing side, an effective transition was made to a new custody bank, which handles the nuts and bolts of investment transactions. Investment accounting was moved to an outside organization, creating greater efficiency in all accounting functions. Finally, investment liquidity was closely monitored to ensure enough available cash flow to pay claims quickly.

On the performance side, close contact was maintained with our investment manager and investment consultant to maximize total returns in a volatile interest environment. The result was favorable returns compared with comparable investment portfolios.

Surplus was also tracked closely to maximize outstanding balances. Net surplus for both Housing Authority Risk Retention Group (HARRG) and Housing Authority Property Insurance (HAPI) surpassed levels defined by regulatory formulas.

In day-to-day business, the finance department worked closely with the underwriting and claims departments to ensure timely receipt of premiums and deductibles. To facilitate this goal, improved information on billing issues was made available to members. When payment delays did occur, there was better follow-up than in the past. The result was a significant decrease in late payments.

There was also increased effort to control the company's operating expenses. Monthly expense reports comparing actual expenditures to planned expenditures were used to help managers stay within budget. The result was overall expense levels that were below plan and more consistent with the lower premium levels charged in recent years.

Of course nothing has a greater impact on money leaving the company than claims paid. The claims staff provided Housing Authority Insurance with another year of efficient claims handling. Claims audit results for 1999 were excellent. The auditors ranked HARRG in the



At Capital Woods in Albany, NY, they've traded in their weather-beaten shingles for weather-resistant siding. And the interior is as modern as they come.

top 10% of public entity organizations in terms of quality and service.

In 1999, HARRG members filed 1,985 general liability claims. For that period, 1,630 claims were closed. HARRG's total paid and reserved losses since inception of the program exceed \$167,000,000. At year's end, 2,034 claims remained open.

Also in 1999, staff performed on-site audits of HARRG self-insured accounts (Chicago Housing Authority and the California Housing and Risk Management Association).

In 1999, HAPI members filed 403 property claims. For that period, 451 claims were closed. HAPI's total paid losses since inception of the program exceed \$43,000,000. At year's end, 165 claims remained open.

Despite the competitive market conditions, Housing Authority Insurance finished 1999 in significantly better financial condition than it started.

Harnessing Technology

In the year leading up to Y2K, Housing Authority Insurance spent considerable time and resources creating and improving its technology with the goal of improving organizational efficiency.

Creating an integrated database network has been a work in progress for quite some time. In 1999, many results from this work could be seen. New marketing and claims systems, and the existing finance system were integrated with the central database. A new human resources software system was implemented to improve tracking and reporting capabilities. Conversion of the company's computer network to a Microsoft Windows NT system was completed. All desktop computers were converted to NT workstations with Microsoft Office 97, 64 megabytes of RAM, 100 megabytes per second data transfer capability, and defragmentation software. These improvements will ensure that staff are able to work more quickly and accurately.

HTVN also made major improvements to its technology. The data portion of the network, which allows two-way data transfer between HTVN and its host sites, was converted from a satellite-based system to a semi-private intranet system. The video broadcast portion of the network was moved from the Telstar 402R satellite to the GE3 satellite. The satellite changeover, which gives subscribers access to additional free programming, was executed at no cost to HTVN.

Addressing Y2K

Throughout 1999, there was much talk about the computer disaster that would strike when the year 2000



Many public housing facilities provide more than just a place to live. When you move into the Dwight Street Homes in Jersey City, NJ, you also get a charming neighborhood.



In Denver, CO, you can get job training at the Campus of Learners.

arrived. Throughout 1999, Housing Authority Insurance meticulously executed a Y2K plan to ensure that no such disaster affected this company.

All custom computer programs, hardware and software, as well as business machinery and facility systems were inventoried, analyzed, and when required, updated to compliance with year 2000 standards.

Improving Infrastructure

To provide fast, knowledgeable service in an efficient, professional manner, a company must be willing to invest in its key assets: facilities and staff.

The company's phone system was updated and expanded to accommodate technology requirements and staff increases. All printed materials, office plaques, signs and flags were updated to reflect the new mission and vision statements and the new logo. A disaster recovery site and plan were readied to ensure our continued operation should harm ever come to the company facility.

In 1999, work began on a site development plan for the vacant parcel of land adjacent to our existing

building. The land was purchased by Housing Authority Insurance in 1998. One possible plan includes building a complex to house new HTVN studios, central archives and office space for staff expansion or lease.

As in past years, the staff worked hard to improve itself. The entire marketing, underwriting and risk control staffs have earned their property casualty licenses. All marketing representatives have either earned their public housing management (PHM) certification or are working toward it. Risk control staff members will use their new knowledge to provide coverage reviews.

The desire of the company as a whole to improve can be seen in the 96% completion rate for last year's 89 major goals.

In 1999, Housing Authority Insurance worked to ensure its success in the future. We took good practices and made them better. We made our solid financial position more secure. We used technology to become more efficient. We visited more members than ever.

The end result: We retained more members than ever. We're positioned to grow. We're ready to serve our members as the public housing industry and insurance landscape change in the coming years. ■



In Paterson, NJ, monstrous high-rises have been razed in favor of smaller, more attractive developments.



As the public housing industry continues to change, Housing Authority Insurance will continue to meet its changing needs.

Housing Authority Insurance Board of Directors and Committees



Barry Romano
Chairman of the Board

Dan Labrie
Chief Executive Officer

Lee Reno
General Counsel



Officers

(Left to Right): Richard Collins, 3RD VICE CHAIR;
John McAvaddy, 1ST VICE CHAIR; Barry Romano, CHAIR;
Douglas Dzema, 2ND VICE CHAIR



Board of Directors

(Left to Right) Top Row: W. James Rice; David Tanenhaus; Arlene Hinson;
Stuart Hughes; Harry House
Middle Row: Richard Collins, 3RD VICE CHAIR; Michael Meyer; Virgil Tinklenberg;
John Primmer; Domenic Schiano; Douglas Dzema, 2ND VICE CHAIR
Bottom Row: John McAvaddy, 1ST VICE CHAIR; R. Glen Redding;
Barry Romano, CHAIR; Jack Womack
Not in Photo: Melvin Brazier; Eric Brown; John Nelson



Nominating Committee

(Left to Right): Alan Katz; Douglas Dzema, CHAIR; Richard Collins;
W. James Rice, VICE CHAIR; Virgil Tinklenberg
Not in Photo: Eric Brown; Debra Sable



Claims Committee

(Left to Right): W. James Rice; Douglas Dzema; Michael McInnish; Kathleen Sulsky; Thomas Hannen
Not in Photo: Eric Brown, CHAIR; Debra Sable, VICE CHAIR; Marisol Avila; LaVerne Boyd; Gillian Brown; Frank Cannatelli; Randy Phillips; Jay Rubin; Kathleen Lynch



Council of Advisors

(Left to Right) Top Row: John Glowacki; Tommie Denson; Thomas Hannen; Tracey Barlow; Art Spence
Bottom Row: Steve Falek; Alan Katz; Douglas Dzema, VICE CHAIR; Bob Neill; John McAvaddy, CHAIR
Not in Photo: Pat Brewer; Vivian Bryant; John Collier; Ernie Etuk; Joseph Finnerty; Terri Hamilton; Eugene Jones; Rodolfo Rangel; Russell Sciandra; William Smith



Underwriting Committee

(Left to Right): Bob Braun; Harry House, CHAIR; Edward Schwartz; Jack Womack; R. Glen Redding; Bob Neill; Dennis Morgan; Tom Hickey
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Finance Committee

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Bottom Row: John Glowacki, VICE CHAIR; Virgil Tinklenberg; Alan Katz; James DiPaolo; Stuart Hughes, CHAIR
Not in Photo: Melvin Braziel; Vivian Bryant; Laura Hinchey-Holly; Lawrence Jackson; Harish Krishnarao; Daniel Rodriguez; Joane Wolpin



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(Left to Right) Top Row: Scott Bertrand; Arlene Hinson; John Smolk; Lee Eastman; Earl Williams
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 Bottom Row: Raymond L'Atrelli; Victoria Adams; Rosa Torres; Marcia Wood Reitz; Domenic Schiano, CHAIR; Steve Falek
 Not in Photo: Deborah Baumgartner; Raymond Budd; Keenan Colquitt; Ernie Etuk; Robert Henderson; Bonnie Latting; Richard L'Europa; David (Joe) Sanders; William Smith



Marketing Committee

(Left to Right) Top Row: James DiPaolo; Alan Katz; Thomas Hannen; David Tanenhaus
 Middle Row: Scott Bertrand; L. Glen Redding; Douglas Dzema; Jack Womack
 Bottom Row: Virgil Tinklenberg, CHAIR; Marcia Wood Reitz; John McAvaddy; Dennis Morgan
 Not in Photo: Steve Falek, VICE CHAIR; Keenan Colquitt; Joseph Garza



Governance Committee

(Left to Right): Richard Collins; David Tanenhaus; John McAvaddy; John Primmer, CHAIR; Barry Romano; Virgil Tinklenberg; Jack Womack; Douglas Dzema
 Not in Photo: Eric Brown



Learning Technologies Committee

(Left to Right) Top Row: Bob Neill; Lee Eastman; W. James Rice; David Tanenhaus, CHAIR
 Bottom Row: Richard Collins; James DiPaolo; L. Glen Redding; Marcia Wood Reitz, VICE CHAIR; John McAvaddy; Jack Womack
 Not in Photo: Eric Brown; Daniel Rodriguez; Lezlie Thompson

Housing Authority Insurance Staff

Executive Services

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Bill Lewellyn, EXECUTIVE VICE PRESIDENT
Leslie Whitlock, DIRECTOR,
EXECUTIVE SERVICES
Glenn Jurgen, HUMAN RESOURCES
COORDINATOR
Michael O'Hearn, COMMUNICATIONS
SPECIALIST
Miriam Robinson, EMPLOYEE BENEFITS
ADMINISTRATOR
Lisa Krasnow, GRAPHIC SPECIALIST
Esther Lerner, RECEPTIONIST

Learning Technologies

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LEARNING TECHNOLOGIES
Jackie Festa-Biega, DIRECTOR OF
PROGRAMMING
Patrick Sullivan, STUDIO DIRECTOR
Jay Dantscher, ASSISTANT STUDIO
DIRECTOR
Paula Shemchuk, PROGRAMMING
ASSISTANT

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Estelle Doolittle, MARKETING
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AND CONSULTING
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Sylvia Malinski, SENIOR RISK CONTROL
ASSOCIATE
Ann Straut-Esden, SENIOR RISK CONTROL
ASSOCIATE
Brian Hunter, SENIOR RISK CONTROL
ASSOCIATE
Brian Whalen, SENIOR RISK CONTROL
ASSOCIATE
Nancy Swistak, ADMINISTRATIVE ASSISTANT
Nancy Quiles, PROGRAM ASSISTANT

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Rita Wade, PROPERTY CLAIMS MANAGER
Dottie Brown, REGIONAL CLAIMS MANAGER
John Weber, REGIONAL CLAIMS MANAGER
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Lynda Houle, CLAIMS EXAMINER
Laura Franco, CLAIMS EXAMINER
Michael Pepe, CLAIMS EXAMINER
Kimberly Clifford, CLAIMS EXAMINER
Karen Bassett, CLAIMS EXAMINER
Stefanie Warner, CLAIMS EXAMINER
Joyce Coleman, SENIOR ADMINISTRATIVE
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Sharon Sciascia, CLAIMS ASSISTANT
Janelle Howard, CLERICAL ASSISTANT

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Gibriel Cham, SPECIAL SERVICES MANAGER
Linda Blanc, SENIOR UNDERWRITER
Jodi Barbieri, SENIOR UNDERWRITER
Ken Merrifield, SENIOR UNDERWRITER
Jean Solla, UNDERWRITER
Cindy Oneto, UNDERWRITER
Karen Hinton, UNDERWRITER
Maurie Wray, ASSISTANT UNDERWRITER
Maria Diaz, ASSISTANT UNDERWRITER
Jeanne Aransky, ASSISTANT UNDERWRITER
Angela Cadacy, ASSISTANT UNDERWRITER
Jane Renauld, INSURANCE SERVICES
REPRESENTATIVE
Fung Shan, INSURANCE SERVICES
REPRESENTATIVE
Debbie Bower, INSURANCE SERVICES
REPRESENTATIVE
Brandi Feero, ADMINISTRATIVE ASSISTANT
Jonna Krish, ADMINISTRATIVE ASSISTANT

Finance/MIS

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Janine Lehr, CONTROLLER
Tracey Gragnano, STAFF ACCOUNTANT
Dorothy Robinson, STAFF ACCOUNTANT
Sun Dutcher, ACCOUNTING ASSISTANT
Ying Xu, ACCOUNTING ASSISTANT
April Parsons, DIRECTOR, MIS
Jonathan Cottle, SENIOR SOFTWARE
ENGINEER
Lucille Tortora, NETWORK MANAGER
Jill McNamee, SYSTEMS ADMINISTRATOR
Lori Harris, HELP DESK SUPPORT SPECIALIST

In addition to the many staff members who helped put this report together, a number of people associated with our member authorities also lent a hand:

Carol E. Gladis, Paterson Housing Authority
Steve Falek, Milwaukee Housing Authority
Ray Budd, Jersey City Housing Authority
Jim DiPaolo, Denver Housing Authority
Barry Romano, Albany Housing Authority
Frank Hillebrandt, Albany Housing Authority
Jackie Zilton, St. Petersburg Housing Authority

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Doug Dzema, Perth Amboy Housing Authority
Brett Linker, Architects Unlimited PC (Perth Amboy)
Chun Y Lai, Chun Y Lai Photography, Perth Amboy
Photos (Cover)

Financial Statements and Independent Auditors' Report

As of and for the years ended December 31, 1999 and 1998

The Board of Directors
Housing Authority Risk Retention Group, Inc.

We have audited the accompanying balance sheets of Housing Authority Risk Retention Group, Inc., as of December 31, 1999 and 1998, and the related statements of net income, changes in members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Housing Authority Risk Retention Group, Inc., as of December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

Saslow, Lufkin & Buggy, LLP

February 25, 2000

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	1999	1998
Assets		
Investments:		
Available for sale – at fair value	\$ 116,802,608	\$ 117,968,443
Investment in HIG	401,198	581,198
Investment in HAPI	275,000	275,000
Total investments	117,478,806	118,824,641
Cash and cash equivalents	5,254,030	8,690,549
Reinsurance recoverables	16,517,493	11,259,320
Prepaid reinsurance premiums	1,209,867	867,823
Premiums receivable (net of allowance for bad debts of \$22,358 in 1999 and \$119,186 in 1998)	2,605,866	3,152,487
Deductible payments receivable (net of allowance for bad debts of \$23,526 in 1999 and \$39,930 in 1998)	494,897	806,231
Accrued investment income	1,584,090	1,785,640
Property and equipment, net	2,829,338	3,037,643
Other assets	1,798,451	1,518,329
Total assets	\$ 149,772,838	\$ 149,942,663
Liabilities and Members' Equity		
Unpaid losses and loss adjustment expenses	\$ 92,660,523	\$ 91,707,328
Unearned premiums	9,981,062	10,156,837
Reinsurance balances payable	2,575,005	452,061
Deferred income	2,402,000	—
Accrued policyholder dividend	3,070,395	2,000,000
Members' equity refund payable	1,867,562	1,867,562
Accrued expenses and other liabilities	3,009,093	3,437,558
Total liabilities	115,565,640	109,621,346
Members' equity:		
Members' contributions	8,017,861	7,714,432
Accumulated other comprehensive (loss) income	(6,400,832)	2,181,457
Retained earnings:		
Designated	967,694	967,694
Undesignated	31,622,475	29,457,734
Total members' equity	34,207,198	40,321,317
Total liabilities and members' equity	\$ 149,772,838	\$ 149,942,663
<i>The accompanying notes are an integral part of these financial statements.</i>		

	1999	1998
Revenues:		
Premiums earned	\$ 21,196,664	\$22,375,357
Ceded premiums earned	(4,636,413)	(2,961,553)
Net earned premiums	16,560,251	19,413,804
Investment income (net of expenses of \$255,606 in 1999 and \$178,738 in 1998)	7,486,726	7,313,668
Net realized investment (losses) gains	(701,922)	20,874
Other	218,891	134,182
Total revenues	23,563,946	26,882,528
Expenses:		
Losses and loss adjustment expenses	13,445,493	17,649,460
Salaries and other compensation	2,392,980	2,144,778
Contractual services/professional fees	1,038,717	879,821
General and administrative	687,887	1,407,592
Policy acquisition costs	679,000	710,000
Risk control & member education	389,248	298,785
Total expenses	18,633,325	23,090,436
Net income before policyholder dividend	4,930,621	3,792,092
Policyholder dividends	(3,000,000)	(2,000,000)
Reversal of prior year policyholder dividends	356,197	595,318
Net income	\$ 2,286,818	\$ 2,387,410
<i>The accompanying notes are an integral part of these financial statements.</i>		

	Members' Contributions	Accumulated Other Comprehensive Income (Loss)	Retained Earnings		Total
			Designated	Undesignated	
Balance at December 31, 1997	\$ 7,448,607	\$ (741,252)	\$ 967,694	\$ 27,070,324	\$ 34,745,373
Comprehensive income:					
Net income	—	—	—	2,387,410	2,387,410
Unrealized holding gains	—	2,943,583	—	—	2,943,583
Less: reclassification adjustment for gains included in net income	—	(20,874)	—	—	(20,874)
Other comprehensive income	—	2,922,709	—	—	2,922,709
Comprehensive income	—	—	—	—	5,310,119
Members' contributions, net	265,825	—	—	—	265,825
Balance at December 31, 1998	7,714,432	2,181,457	967,694	29,457,734	40,321,317
Comprehensive loss:					
Net income	—	—	—	2,286,818	2,286,818
Unrealized holding losses	—	(9,284,211)	—	—	(9,284,211)
Add: reclassification adjustment for losses included in net income	—	701,922	—	—	701,922
Other comprehensive loss	—	(8,582,289)	—	—	(8,582,289)
Comprehensive loss	—	—	—	—	(6,295,471)
Equity dividends	—	—	—	(122,077)	(122,077)
Members' contributions, net	303,429	—	—	—	303,429
Balance at December 31, 1999	\$ 8,017,861	\$ (6,400,832)	\$ 967,694	\$ 31,622,475	\$ 34,207,198
<i>The accompanying notes are an integral part of these financial statements.</i>					

	1999	1998
Cash flows from operating activities:		
Net income	\$ 2,286,818	\$ 2,387,410
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	340,722	379,364
Net realized investment losses (gains)	701,922	(20,874)
Amortization and accretion on investments, net	100,401	34,692
Loss on investment in HIG	180,000	352,018
Changes in assets and liabilities:		
Reinsurance recoverables	(5,258,173)	(502,679)
Prepaid reinsurance premiums	(342,044)	140,878
Premiums receivable	546,621	445,837
Deductible payments receivable	311,334	139,750
Accrued investment income	201,550	(358,702)
Other assets	(280,122)	(244,631)
Unpaid losses and loss adjustment expenses	953,195	4,027,806
Unearned premiums	(175,775)	59,713
Reinsurance balances payable	2,122,944	213,373
Deferred income	2,402,000	—
Accrued policyholder dividend	1,070,395	(500,000)
Accrued expenses and other liabilities	(428,466)	1,025,395
Net cash provided by operating activities	4,733,322	7,579,350
Cash flows from investing activities:		
Purchases of available for sale securities	(35,840,792)	(63,386,146)
Proceeds from investments sold or matured	22,394,144	46,745,886
Investment repayments	5,227,872	7,765,333
Investment in HIG	—	(249,305)
Additions to property and equipment	(132,417)	(469,541)
Net cash used in investing activities	(8,351,193)	(9,593,773)
Cash flows from financing activities:		
Principal repayments on long-term debt	—	(66,667)
Equity dividends	(122,077)	—
Members' contributions	303,429	265,825
Net cash provided by financing activities	181,352	199,158
Net decrease in cash	(3,436,519)	(1,815,265)
Cash and cash equivalents, beginning of year	8,690,549	10,505,814
Cash and cash equivalents, end of year	\$ 5,254,030	\$ 8,690,549
Supplemental disclosure:		
Cash paid during the year for interest	\$ —	\$ 486
<i>The accompanying notes are an integral part of these financial statements.</i>		

NOTE 1 GENERAL

Reporting Entity — Housing Authority Risk Retention Group, Inc. (the Company or HARRG) was incorporated on March 20, 1987, under the laws of the State of Vermont. It is a nonprofit risk retention group formed for the purpose of providing liability insurance coverage to member public housing authorities (member PHAs) throughout the United States.

Concentrations — The Company provides liability insurance to member PHAs, which are governed and funded by the U.S. Department of Housing and Urban Development. Certain changes in public policy and/or funding of member PHAs could have a significant impact on the operations of the Company.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments — The Company accounts for investments in accordance with Statement of Financial Accounting Standards No. 115 (FAS 115), *Accounting for Certain Investments in Debt and Equity Securities*. The Company's management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. At December 31, 1999 and 1998, all of the Company's investments are classified as available for sale and are carried at fair value. Unrealized gains and losses relating to available for sale securities are reported as a separate component of members' equity as accumulated other comprehensive income (loss). Realized investment gains and losses are determined on a specific identification basis.

The amortized costs of fixed maturities are adjusted for amortization of premiums and accretion of discounts. Such amortization and accretion are included in interest income.

Within the mortgage-backed securities portfolios, the Company invests in collateralized mortgage obligations and mortgage-backed security pools. Each security carries a varying degree of prepayment and interest risk, which can impact the fair value and the ultimate amount of investment income earned. Acceleration or deceleration of prepayments of the underlying mortgages can be caused by interest rate changes.

The fair values of investments are measured using quoted market prices or dealer quotations, when available. When quoted market prices are not available, fair value is measured using quoted market prices for similar securities.

The investment in Housing Investment Group, Inc. (HIG) is accounted for under the equity method of accounting (see Note 6).

The investment in Housing Authority Property Insurance, Inc. (HAPI) is carried at cost.

Cash and Cash Equivalents — For financial statement purposes, the Company considers all short-term investments with an original maturity of three months or less to be cash equivalents. For these short-term investments, the carrying amount is an estimate of market value. Additionally, HARRG maintains cash balances at several banks. Accounts at each institution are insured by the Federal Deposit Insurance Corporation up to \$100,000.

Policy Acquisition Costs — Policy acquisition costs, which primarily consist of commissions, underwriting fees and premium taxes, are expensed as incurred.

Property and Equipment — Property and equipment are recorded at cost and are depreciated over the estimated useful lives of the assets. Depreciation is computed using the straight-line method for all fixed assets.

Unpaid Losses and Loss Adjustment Expense Reserves — Unpaid losses and loss adjustment expense reserves represent estimated provisions for both reported and unreported claims incurred and related expenses. In determining unpaid losses and loss adjustment expense reserves, the Company annually reviews its overall position, its reserving techniques and its reinsurance. These reserves represent the estimated ultimate cost of all incurred claims and claim adjustment expenses. Since the reserves are based upon estimates, the ultimate liability may be more or less than such reserves. The effects of changes in such estimated reserves are included in the results of operations in the period in which the estimates are changed. Such changes may be material to the results of operations and could occur in a future period.

Revenue Recognition — Premiums are generally recognized as revenue on a pro rata basis over the policy term. The portion of premiums that will be earned in the future are deferred and reported as unearned premiums.

Under certain reinsurance agreements, the Company receives a commission on premiums it cedes to reinsurers. Commissions are earned over the terms of the underlying policies to which they relate.

Reinsurance — In the normal course of business, the Company seeks to reduce losses by reinsuring certain levels of risk with reinsurers. Amounts recoverable from reinsurers are estimated in a manner consistent with the reinsurance contracts. Such reinsurance is applicable on a per policy basis, generally to those policies issued by the Company with occurrence limits in excess of \$1 million and up to \$5 million for liability coverage.

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

Fair Values of Financial Instruments — The Company values financial instruments as required by Statement of Financial Accounting Standards No. 107, *"Disclosure about Fair Value of Financial Instruments."* The carrying amount of cash, premiums receivable, other assets, accounts payable and other liabilities approximate fair value.

Reclassifications — Certain reclassifications to the 1998 financial statements have been made in order to conform with the 1999 presentation. Such reclassifications did not have a material effect on the financial statements.

Comprehensive Income — During 1998, the Company adopted Financial Accounting Standards Board Statement 130, *"Reporting Comprehensive Income."* Comprehensive income (loss) is a measurement of certain changes in members' equity that result from transactions and other economic events other than transactions with members. For the Company, these consist of changes in unrealized gains and losses on the investment portfolio, which are used to adjust net income to arrive at comprehensive income (loss). The cumulative amount of these changes is reported in the balance sheets within accumulated other comprehensive income (loss).

NOTE 3 INVESTMENTS

Fixed maturities classified as available for sale and carried at fair value as of December 31, 1999 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	\$ 964,090	\$ —	\$ (11,235)	\$ 952,855
State and political subdivisions	11,549,939	66,386	(669,505)	10,946,820
Corporate bonds	59,079,052	52,334	(3,049,727)	56,081,659
Mortgage-backed securities	49,587,139	9	(2,628,676)	46,958,472
Foreign government securities	2,023,220	11	(160,429)	1,862,802
Total available for sale	\$123,203,440	\$ 118,740	\$ (6,519,572)	\$ 116,802,608

Fixed maturities classified as available for sale and carried at fair value as of December 31, 1998 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	\$ 7,145,127	\$ 265,392	\$ —	\$ 7,410,519
State and political subdivisions	10,930,712	557,553	(18,326)	11,469,939
Corporate securities	55,684,665	2,026,294	(527,415)	57,183,544
Mortgage-backed securities	42,026,482	456,295	(578,336)	41,904,441
Total available for sale	\$115,786,986	\$ 3,305,534	\$ (1,124,077)	\$ 117,968,443

The cost and fair value of fixed maturities are shown by contractual maturity as of December 31, 1999. 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.

	Amortized Cost	Fair Value
Due to mature:		
One year or less	\$ —	\$ —
After one year through five years	24,373,793	23,881,013
After five years through ten years	41,369,310	38,404,838
After ten years	7,873,198	7,558,285
Mortgage-backed securities	49,587,139	46,958,472
Total fixed maturities	\$123,203,440	\$116,802,608

Proceeds from sales and repayments of securities classified as available for sale amounted to \$27,622,016 and \$54,511,219 in 1999 and 1998, respectively. Gross gains of \$364,973 and \$912,565, and gross losses of \$566,895 and \$891,691 were realized on those sales during 1999 and 1998, respectively.

In 1999 the Company recorded a \$500,000 realized loss for the permanent impairment of a collateralized mortgage obligation. At December 31, 1999, the security had an adjusted cost basis of \$1,494,313 and a fair market value of \$1,160,000.

NOTE 4 PROPERTY AND EQUIPMENT

The useful life, cost, accumulated depreciation, and book value for the Company's property and equipment are presented in the following tables:

December 31, 1999	Useful Life	Cost	Accumulated Depreciation	Book Value
Land		\$ 618,232	\$ —	\$ 618,232
Building	31 years	2,400,583	(465,474)	1,935,109
Furniture and fixtures	5 years	637,277	(595,156)	42,121
EDP equipment	3 years	2,067,893	(1,834,017)	233,876
		\$ 5,723,985	\$ (2,894,647)	\$ 2,829,338

December 31, 1998				
Land		\$ 618,232	\$ —	\$ 618,232
Building	31 years	2,399,176	(388,114)	2,011,062
Furniture and fixtures	5 years	728,011	(653,971)	74,040
EDP equipment	3 years	2,015,197	(1,680,888)	334,309
		\$ 5,760,616	\$ (2,722,973)	\$ 3,037,643

Depreciation expense for the years ended December 31, 1999 and 1998 was \$340,722 and \$379,364, respectively. Approximately \$156,000 and \$178,000 in 1999 and 1998, respectively, is allocated to the other entities per the management services agreement as disclosed in Note 6.

NOTE 5 INCOME TAXES

The Company has received a determination letter from the Internal Revenue Service indicating that the Company qualifies under the provisions of Section 115 of the Internal Revenue Code and is exempt from federal income taxes.

NOTE 6 RELATED PARTY TRANSACTIONS

In June 1995, the Company and Housing Authority Property Insurance, Inc. (HAPI) formed Housing Investment Group, Inc. (HIG) to serve as a for-profit holding company to govern the related businesses to which the Company and HAPI have an ownership interest. HIG has two classes of stock, a voting class (Class A) which is owned 50% by the Company and 50% by HAPI and a non-voting class (Class B) which was initially owned 75% (9,000 shares Class B stock) by the Company and 25% (3,000 shares Class B stock) by HAPI. The ownership of the non-voting shares fluctuates based upon the relative capital bases of the Company and HAPI. The investment in HIG is accounted for under the equity method of accounting.

At December 31, 1999 and 1998, the Company owned 74% and 75% (8,860 and 9,000 shares of Class B stock) and HAPI owned 26% and 25% (3,140 and 3,000 shares of Class B stock), respectively.

The Company provides management services to HAPI, Housing Telecommunications, Inc. (HTI), Housing Insurance Services, Inc. (HIS) and Housing Authority Insurance, Inc. (HAI) on a fee-for-service basis, which is reimbursed to the Company and reduces its general and administrative expenses. The cost of these services is directly allocated to these entities. Effective January 1, 1999, the Company began to allocate costs to Housing Investment Group, Inc (HIG) and Satellite Telecommunications, Inc. (STI). The approximate amounts of allocated costs and the related accounts receivable, reflected in other assets, are as follows:

	Allocated Costs		Accounts Receivable	
	1999	1998	1999	1998
HAPI	\$ 2,690,000	\$ 2,350,000	\$ 566,000	\$ 579,000
HTI	367,000	401,000	36,000	98,000
HIS	165,000	86,000	20,000	16,000
HAI	78,000	56,000	6,500	12,000
HIG	23,000	—	36,000	—
STI	54,000	—	12,000	—
Total	\$ 3,377,000	\$ 2,893,000	\$ 676,500	\$ 705,000

The Company contracts with HAI to provide marketing services on behalf of HARRG. The Company recognized an expense for these services of \$120,840 and \$97,500 for the years ended December 31, 1999 and 1998, respectively.

The Company also has a service agreement with Housing Environmental Services, Inc. (HES), (a wholly owned subsidiary of HIG), whereby HES provides risk management services in return for a percentage of the Company's monthly earned premium on lead-based paint coverage. For the years ended December 31, 1999 and 1998, the Company incurred expenses of \$27,651 and \$90,688, respectively.

The Company entered into an agreement with HTI to support the delivery of risk management training to members. The Company recognized an expense of \$192,000 and \$90,000 for fees paid to HTI for the year ended December 31, 1999 and 1998, respectively.

NOTE 7 EMPLOYEE BENEFITS

The Company maintains a defined contribution pension plan covering substantially all of its employees. Employees are eligible to participate in the plan on the first day of the month after they reach the age of 21. The Company contributes 10% of an employee's compensation on a monthly basis. Employees are unable to contribute to the plan. The plan had immediate vesting for any employee who was employed and eligible to participate prior to March 1, 1992. Vesting for all persons employed after March 1, 1992 is on a graduated schedule of 60% at the end of the third year of employment, 80% at the end of the fourth year of employment, and 100% at the end of the fifth year of employment. Total expense for the years ended December 31, 1999 and 1998, was \$166,417 and \$145,626, respectively.

Effective November 1, 1999, the Company is the sponsor of the Housing Authority Risk Retention Group 401(k) Plan, (the "Plan"). All employees 21 years or older and who have completed one year of service are eligible to participate in the Plan. The Company does not match employee contributions. Administration expenses for the Plan are paid for by the Company.

NOTE 8 MEMBERS' EQUITY

The Company is owned by its members and each member makes an initial capital contribution upon membership. The membership agreement requires each member to remain a member for a minimum of three years. If a member withdraws prior to the three-year period, the member forfeits its initial surplus contribution and any additional surplus contributions. If a member withdraws subsequent to the three-year period, other than as a result of certain specified events, it may either (1) withdraw its initial and any additional surplus contributions as defined by the membership agreement with such withdrawal to be completed at the discretion of the Board of Directors but not later than five years from the date of expiration, or (2) maintain its surplus account with the Company, in which case it shall share in all allocations to and from surplus accounts as if it continued to be a member. Distributions can be at the earliest of the following three circumstances: (1) the close of all claims from the policy years in which the member participated, (2) the discretion of the Board of Directors, or (3) in the event of the liquidation of the Company.

HARRG is required by the Vermont Department of Banking, Insurance, Securities and Health Care Administration to maintain a minimum statutory surplus of \$500,000.

As of December 31, 1999 and 1998, there were member PHAs that had withdrawn their membership in the Company, however, they have not formally requested a distribution of their surplus accounts. Should these members request a distribution of their surplus accounts, the Company will return the amounts in accordance with the provisions of the membership agreement and the policy on member withdrawal as described above, and will classify the amounts as a liability within the balance sheet. As of December 31, 1999 and 1998, two members had requested a distribution of their surplus accounts; accordingly, \$1,867,562 has been reclassified from members' equity to members' equity refund payable.

The Company provides its members with discretionary policyholder dividends, which are calculated based upon the underwriting experience of each member and the 50% capital contribution, and are reflected as policyholder dividends in the statement of net income. Policyholder dividends of \$3,000,000 and \$2,000,000 were accrued for the years ended December 31, 1999 and 1998. In 1999 and 1998, the Company reversed \$356,197 and \$595,318, respectively, of accrued policyholder dividends due to PHAs that withdrew membership in the Company and thereby disqualified themselves from receiving policyholder dividends.

The Company provides its members with equity dividends to the extent that they are utilized to purchase satellite equipment from HTI. Equity dividends amounted to \$122,077 in 1999. There were no equity dividends in 1998.

The Company's Board of Directors designated retained earnings of \$967,694 in 1992 for the acquisition of land and construction of a building to be used for HAPI and the Company's offices.

NOTE 9 STATUTORY ACCOUNTING PRACTICES

The Vermont Department of Banking, Insurance, Securities and Health Care Administration (the Department) recognizes as net income and members' equity those amounts determined in conformity with statutory accounting practices prescribed or permitted by the Department, which differ in certain respects from generally accepted accounting principles. The amounts of statutory net income were approximately \$4,680,000 and \$2,387,000 for the years ended December 31, 1999 and 1998, respectively. The amounts of statutory surplus were approximately \$42,107,000 and \$36,893,000 as of December 31, 1999 and 1998, respectively. Pursuant to the laws of the State of Vermont, the Company's dividend payments are limited to the lesser of 10% of statutory surplus or net income excluding realized capital gains.

In 1998, the National Association of Insurance Commissioners (NAIC) adopted the Codification of Statutory Accounting Principles guidance, which will replace the current Accounting Practices and Procedures manual as the NAIC's primary guidance on statutory accounting. The NAIC has recommended an effective date of January 1, 2001. The Company has not estimated the potential effect of the Codification guidance if adopted by the Vermont Department of Banking, Insurance, Securities and Health Care Administration.

NOTE 10 INSURANCE ACTIVITY

The Company has entered into reinsurance contracts with other insurance companies in order to reduce its exposure to large losses by permitting recovery of a portion of losses from reinsurers. These contracts do not discharge the primary liability of the Company as direct insurer of those risks reinsured. The Company evaluates the financial condition of potential reinsurers and continually monitors the financial condition of the present reinsurers. Additionally, the Company evaluates current and prospective reinsurers as to concentrations of credit risk arising from similar activities or economic characteristics in order to minimize exposure to significant losses resulting from reinsurer insolvencies. Through June 30, 1998, the general liability reinsurance program had numerous reinsurers participating in the various levels of retention which generally are rated A- or better.

Through June 30, 1998, the reinsurance for general liability and public officials' liability, ceded on an excess basis, provides for a series of layers subject to annual occurrence limits totaling \$4,000,000 above the Company's primary retention of \$1,000,000. In addition, the Company participates on a quota share basis excess of the \$2,000,000 occurrence limit. In the event that the annual per occurrence reinsurance limit is exhausted because of losses, a \$4,000,000 per occurrence limit can be reinstated, for an additional premium, subject to an aggregate limit of \$7,000,000 to provide for \$11,000,000 in reinsurance protection in any one year.

Effective July 1, 1998, the Company entered into a reinsurance agreement with General Reinsurance Company, which provides for \$4,000,000 of coverage in excess of the Company's \$1,000,000 retention. Reinstatements are free and are unlimited.

On June 1, 1998, the Company entered into a retrospective reinsurance agreement for the New York City Housing Authority (NYCHA) book of business, which was written from June 1, 1987 to June 1, 1995. The agreement provides for coverage of 90% of all net losses and allocated loss adjustment expenses of \$5,000,000 excess of \$19,750,000 of ultimate net loss. The agreement also provides coverage of 90% of \$4,000,000 excess of \$25,054,095, however, additional premium will be required in this layer according

to provisions in the contract. The agreement is accounted for under the provisions of FAS 113, *"Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts."* As of December 31, 1999 and 1998, the Company had recognized reinsurance recoverables and deferred income of \$2,402,000 and \$0, respectively.

In 1999, the Company obtained reinsurance from HAPI under an aggregate excess of loss reinsurance agreement. The agreement provides for reinsurance protection to HARRG for all losses in excess of HARRG's retention, which was \$7,400,000 for the period July 1, 1999 to December 31, 1999. The agreement also provides for an individual coverage period and overall aggregate limit which was \$3,300,000. The agreement provides for deferred payment for a portion of the reinsurance premium, which was \$1,803,255 for the year ending December 31, 1999. The Company also has recorded ceding commission income of \$346,823 and a reinsurance recoverable of \$973,409 for the year ending December 31, 1999.

Premiums written and related reinsurance amounts for the years ended December 31, 1999 and 1998, are summarized as follows:

	Premiums Written		Premiums Earned	
	1999	1998	1999	1998
Direct premiums	\$19,683,667	\$21,229,498	\$19,888,610	\$21,177,863
Premiums assumed	1,337,222	1,205,572	1,308,054	1,197,494
Premiums ceded	(4,978,457)	(2,820,675)	(4,636,413)	(2,961,553)
Net premiums	\$16,042,432	\$19,614,395	\$16,560,251	\$19,413,804

The Company recorded reinsurance recoveries of \$4,230,611 and \$568,334 in 1999 and 1998, which is reflected as a reduction in losses and loss expenses incurred in the Statements of Net Income.

A reconciliation of changes in unpaid losses and loss adjustment expenses for the years ended December 31, 1999 and 1998, are summarized as follows (in thousands):

	1999	1998
Balance at beginning of year	\$91,707	\$87,680
Less reinsurance recoverables	(11,259)	(10,757)
Incurred related to:		
Current year	9,550	15,627
Prior years	4,634	828
Total incurred	14,184	16,455
Paid related to:		
Current year	(405)	(412)
Prior years	(14,520)	(12,518)
Total paid	(14,925)	(12,930)
Net balance at end of year	79,707	80,448
Plus reinsurance recoverables	12,953	11,259
Balance at end of year	\$92,660	\$91,707

As a result of changes in estimates of insured events in prior years, the provision of claims and claim adjustment expenses increased by approximately \$4,600,000 and \$828,000 in 1999 and 1998, respectively. The loss development trend is within the normal range for the industry.

NOTE 11 COMMITMENTS AND CONTINGENCIES

In December 1996, the Company approved the issuance of a \$771,000 line of credit to HTI. During 1998, HTI borrowed \$470,000. Interest, which is being charged at the prime rate, amounted to \$39,950 and \$13,467 in 1999 and 1998, respectively.

In 1998, the Company established a \$2,000,000 line of credit with First Union National Bank for purposes of meeting short-term operating cash requirements. Amounts drawn down against the line will incur interest charges at the prime rate plus 1%. There were no outstanding balances at December 31, 1999 and 1998.

Management's Discussion and Analysis

For the years ended December 31, 1999 and 1998

THE COMPANY — AN OVERVIEW

Housing Authority Risk Retention Group, Inc. (The Company or HARRG) was incorporated on March 20, 1987 as a mutual captive insurer. HARRG provides liability insurance to member housing authorities throughout the United States. HARRG is a nonprofit, federal tax-exempt company owned by member public housing authorities (PHAs) and operates pursuant to the Federal Liability Risk Retention Act of 1986.

HARRG was developed as a result of the inability of many PHAs to obtain liability coverage or to obtain such coverage at an affordable rate. In response, PHAs established HARRG to provide stable, affordable liability insurance coverage.

Management operations at HARRG include the following functions: claims services, finance, insurance agency, broker and trade association management, marketing, management information systems, interactive learning television programming, risk control and underwriting. As of December 31, 1999, HARRG employed 70 individuals. HARRG also provides management services under contract to Housing Authority Property Insurance, Inc. (HAPI), Housing Telecommunications, Inc. (HTI), Housing Authority Insurance, Inc. (HAI), Satellite Telecommunications, Inc. (STI), Housing Investment Group, Inc. (HIG) and Housing Insurance Services, Inc. (HIS).

HARRG is a niche market insurer. The Company only serves PHAs in the United States. Currently, HARRG underwrites 36% of this market on a per unit basis. HARRG's Board of Directors and various committees review the mission and vision statement at their quarterly meetings and meet annually to update these statements.

In June 1995, HARRG and HAPI formed HIG to serve as a downstream for-profit holding company to govern related businesses to which the Company and HAPI have ownership interest. With the incorporation of HIG, the Company and HAPI consolidated all of the for-profit business entities under the holding company effective January 1, 1996. The subsidiaries include: Housing Insurance Services, Inc. (HIS), (insurance agency), Housing Environmental Services, Inc. (HES) (environmental testing laboratory) and Satellite Telecommunications, Inc. (STI) (satellite telecommunication services).

In 1999, the Company obtained reinsurance from HAPI under an all lines aggregate excess of loss reinsurance agreement. The agreement provides for reinsurance protection to HARRG for all losses in excess of HARRG's defined retention. The contract does provide for coverage period and cumulative limits. This contract is effective through December 31, 2002.

The following discussion provides an assessment by management of the current GAAP financial position, results of operations, cash flow and liquidity, and changes in financial position for HARRG. Information presented in this discussion supplements the financial statements, schedules and exhibits of the 1999 GAAP Audited Financial Statements.

1999 ENVIRONMENT

The U.S. property/casualty market continued to show weak premium growth due to heavy premium price discounting and new competition due to the availability of low cost capital. The existence of state-level

housing authority pools sponsored by insurance agencies has also resulted in increased competition for HARRG. Industry profits in 1999 are projected to show a second year of decline from the record profits recorded by the industry in 1997. The combined ratio is estimated at 108.0% versus 105.6% for 1998 primarily due to the heavy premium discounting and poor workers' compensation results. Reinsurance pricing is beginning to show some signs of modest firming, but dramatic changes in the primary markets are not anticipated until there is a significant depletion of capital.

FINANCIAL POSITION

HARRG total assets at year-end were \$149,772,838, essentially unchanged from 1998's assets of \$149,942,663.

Cash flows from written premiums and sales of securities as discussed later, were directed into the investment portfolio and invested into externally managed fixed income and high yield bond portfolios. Positive cash flows were offset by an \$8,582,289 decline in market value. As a result, the bond portfolio, on a fair value basis, decreased by \$1,165,835 or 1.0% to \$116,802,608 at year-end 1999.

As of December 31, 1998, the Company owned two variable rate securities with a fair value of \$3,705,461. In 1999, one of the securities was sold at a loss of \$123,429. The remaining security has an amortized cost of \$1,494,313 and a market value of \$1,160,000 following recognition of a \$500,000 permanent impairment to the amortized cost in 1999. This holding will be liquidated when market conditions are more favorable.

During 1999, HARRG's investment in HIG decreased by \$180,000 in order to reflect its percentage ownership in the loss of HIG. HIG has two classes of stock, a voting class (Class A) which is owned 50% by the Company and 50% by HAPI and a non-voting class which was initially owned 75% (9,000 Class B shares) by the Company and 25% (3,000 Class B shares) by HAPI. The ownership of the non-voting shares fluctuates based upon the capital bases of the Company and HAPI. At December 31, 1999, the Company owned 74% (8,860 shares) of Class B stock.

Reinsurance recoverables increased from \$11,259,320 at December 31, 1998, to \$16,517,493 at December 31, 1999. The increase reflects payments due from reinsurers on several claims in excess of HARRG's retention level.

Premiums receivable decreased by \$546,621 to \$2,605,866 at December 31, 1999. This decline reflects a reduction of \$1.5 million in General Liability direct premiums written.

In August 1993, HARRG occupied its new home office, which it built and owns. The construction of the building was financed by a five-year term loan of \$2,000,000. The loan was fully secured by readily marketable securities pledged by the Company. At December 31, 1998, HARRG had repaid the full amount of the loan. In 1998, to prepare for potential expansion, HARRG purchased a lot adjacent to the current property at a cost of \$292,000.

Reserves for unpaid losses and loss adjustment expenses at December 31, 1999, reflect the estimate of the liability for the ultimate net cost of reported claims and estimated "incurred but not reported" (IBNR) claims arising from losses which occurred by year's end. The Company has retained an independent actuarial consulting firm to determine the adequacy of loss reserves on an annual basis. At December 31, 1999, reserves for unpaid losses and loss adjustment expenses, including IBNR reserves, were \$92,660,523, an increase of \$953,195 or 1.0% over the 1998 reserve figure of \$91,707,328.

Overall, development on prior year losses was modestly unfavorable due to IBNR strengthening. Attention continued to be paid to claims from one large policyholder currently in runoff. Management also continues to closely monitor and report on claim activities generated from this one insured. The policyholder was insured from July 1, 1987 to June 30, 1995. In order to minimize the severity of future potential liabilities caused by this one insured, management purchased retroactive aggregate excess reinsurance for this account. Based on estimated ultimate losses, a recovery of \$2,402,000 has been recorded as deferred income. In 1999, management conducted an audit of all claims from this one insured that fell within the policy self-insured retention. The result of the claim audit was generally favorable. Accordingly, management believes that loss reserves are appropriately stated at December 31, 1999, based upon available loss data.

All of HARRG's reinsurers are approved in the State of Vermont. Management selects reinsurers who have an A.M. Best rating of at least A- or equivalent rating from other rating agencies. Loss and loss adjustment expense reserves are not discounted. Salvage and subrogation recoveries are not considered when setting reserves.

Unearned premiums were \$9,981,062 at year-end versus \$10,156,837 at December 31, 1998, a decrease of 1.7% or \$175,775. HARRG writes three-year policies, which are annually rated.

In 1999 and 1998, the Company accrued premium credits of \$3,000,000 and \$2,000,000, respectively. Actual distribution of the 1998 accrual was \$1,643,803 resulting in an increase to 1999 income of \$356,197. The \$3,000,000 accrual in 1999 was reflected as a reduction of income and an accrued liability at December 31, 1999.

Capital and surplus declined to \$34,207,198, a decrease of \$6,114,119 or 15.2% from \$40,321,317 at December 31, 1998. The decrease was due to recognition of an unrealized investment loss of \$8,582,289. This was modestly offset by net income in 1999 of \$2,286,818.

RESULTS OF OPERATIONS

Net written premiums for 1999 decreased by 18.2% to \$16,042,432 from \$19,614,395 in 1998. Earned premiums decreased by \$2,853,553 or 14.7% to \$16,560,251 for the year ended December 31, 1999, versus \$19,413,804 for the same period in 1998. Rate reductions in the face of increased competition and premiums ceded as a result of an aggregate stop-loss reinsurance agreement with HAPI accounted for the decrease in written and earned premiums.

Investment income, net of expenses, for the year ended December 31, 1999, was \$7,486,726, an increase of \$173,058 or 2.4% over 1998 income of \$7,313,668. 1999 recorded a realized loss of \$701,922 including the \$500,000 permanent impairment. Investment income was positively impacted by the growth in the bond portfolios, offset somewhat by declining interest rates for new investments.

In the beginning of 1998, the investment portfolios were managed both internally and by an external manager. In March of 1998, the decision was made to move the remaining in-house portfolio and all externally managed funds to Wellington Management Company. Investment policy calls for the portfolio to be managed on a "total rate of return" basis. This concept breaks investment return down into two components: coupon yield and capital appreciation. As a result, realized and unrealized gains or losses from securities transactions are a component of HARRG's investment return.

Loss and loss adjustment expenses incurred totaled \$13,445,493 for the year ended December 31, 1999, versus \$17,649,460 for 1998, down \$4,203,967 or 23.8%. The loss ratio improved to 81.2% from 90.9% reflecting lower general liability losses due to favorable case law and claim settlements, and mild weather conditions throughout the United States. An annual claims audit was performed by an independent consulting firm and the results confirmed that the Company was handling claims in an efficient and professional manner. As part of this audit process, claims reserving practices were reviewed to ascertain that ultimate values are being set on claims.

Operating expenses decreased to \$4,508,832 or 4.7% for the year ended December 31, 1999, from \$4,730,976 for 1998, which included a charge for the employee lawsuit discussed below.

The Company provides management services to HAPI, HTI, HIS, HAI, HIG and STI on a fee-for-service basis, which is reimbursed to the Company and reduces its operating expenses. The cost of these services is being directly allocated to these entities.

In 1999, the Company settled a lawsuit brought by a former employee alleging breach of contract under the terms of an employment agreement which expired on July 13, 1999. The final settlement, which relieves the Company of all future liabilities, was within the amount accrued as part of the 1998 financial statements.

HARRG had net income of \$2,286,818, which was essentially unchanged from 1998's net income of \$2,387,410.

CASH FLOW AND LIQUIDITY

Liquidity can be defined as the Company's ability to generate sufficient cash flows to meet the cash requirements of operations, primarily paying losses and other underwriting expenses. Primary sources of cash include cash flow from operations, i.e., premium income and investment income, cash provided from the sale or maturity of invested assets and capital contributions from members. The Company generated net positive cash flow from operations of \$4,733,322. Net positive cash flows are used to fund commitments and purchase additional investment securities. Cash on hand decreased from \$8,690,549 at December 31, 1998, to \$5,254,030 at December 31, 1999, due to timing differences in the receipt of premium and reinsurance receivables.

In 1998, the Company established a \$2,000,000 line of credit with First Union Bank for purposes of meeting short term operating cash requirements without untimely liquidation of investments. No amounts were drawn down in 1999.

MANAGEMENT INFORMATION SYSTEMS

Considerable time and expense (\$180,000) were directed at ensuring that hardware, custom and vendor software and third-party interfaces would function in 2000. The changeover occurred without interruption to business processes.

Management believes that the effective use of technology is critical to the success of the organization, as the market becomes increasingly competitive. The Company has implemented several customized systems that include Underwriting (rating/quoting, policy issuance), Claims (payments, reserve tracking, and loss reporting), Administration (customer information) and Report Writer (financial reporting). The accounting

system has also been implemented for all companies and is tightly integrated with the customized systems. Work is also progressing in connection with the expanded use of the Internet for the purpose of communicating and sharing information with the Company's policyholders and vendors. Nearly \$425,010 was expended in 1999 for systems development.

BOARD POLICIES AND MANAGEMENT PRACTICES

The Board of Directors of the Company currently requires that certain audits, conducted by independent outside firms, be performed on an annual basis. The 1999 audit schedule included: (1) an actuarial loss certification, submitted as part of the 1999 Annual Statement; (2) a claims audit performed in October 1999; (3) a financial audit for both GAAP and SAP, to be completed by the end of May 2000; (4) an investment audit of performance, conducted quarterly; (5) a claims audit on large policyholders with self-insured retention; (6) an underwriting audit, conducted by the Company's reinsurers prior to year-end; and (7) a review of the risk management program, initiated in 1998 and completed in early 1999.

The Company's policy objective is to break even for underwriting. In 1999, a combined ratio of 112.5% was recorded. The two-year overall combined ratio was 116.0%. The operating ratio for the two-year period, which includes investment results and other income, is 82.7%.

As a captive mutual insurer, the Company's Board of Directors and management have made a significant commitment to risk control. A total of approximately 7.5% or \$389,248 of the Company's administrative expense budget is allocated to training, technical assistance, engineering, and other services designed to reduce member losses.

OPINION

The preceding Management's Discussion and Analysis provides an assessment of the financial position, results of operations, and cash flow and liquidity for the fiscal year ended December 31, 1999, as reported in the 1999 GAAP Audited Financial Statements. Representations made herein are those of management according to the best of their knowledge and belief.

Dated: March 31, 2000

/s/ **Daniel Labrie**

President and Chief Executive Officer

/s/ **Carol Pollack**

CFO & Treasurer

Financial Statements and Independent Auditors' Report

As of and for the years ended December 31, 1999 and 1998

The Board of Directors
Housing Authority Property Insurance, Inc.

We have audited the accompanying balance sheets of Housing Authority Property Insurance, Inc., as of December 31, 1999 and 1998, and the related statements of operations, changes in members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Housing Authority Property Insurance, Inc., as of December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

Saslow, Lufkin & Buzg, LLP

February 25, 2000

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Balance Sheets	Statements of Operations	Statements of Changes in Members' Equity	Statements of Cash Flows	Notes to Financial Statements	Management's Discussion and Analysis
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	1999	1998
Assets		
Investments:		
Available for sale – at fair value	\$ 19,844,728	\$ 19,339,679
Investment in HIG	317,990	317,990
Total investments	20,162,718	19,657,669
Cash and cash equivalents	1,728,258	6,482,894
Premiums receivable	5,051,172	1,418,073
Reinsurance escrow accounts	2,232,261	2,329,944
Reinsurance recoverable	1,348,476	—
Accrued investment income	292,335	240,478
Other assets	689,163	5,027
Due from affiliates	5,507,322	607,322
Total assets	\$ 37,011,705	\$ 30,741,407
Liabilities and Members' Equity		
Unpaid losses and loss adjustment expenses	\$ 15,832,150	\$ 11,192,908
Unearned premiums	5,683,674	4,132,793
Reinsurance payable	1,277,732	—
Accrued expenses and other liabilities	996,157	1,407,163
Due to affiliates	921,093	590,161
Total liabilities	24,710,806	17,323,025
Members' equity:		
Members' contributions	4,615,715	4,637,240
Accumulated other comprehensive (loss) income	(1,060,739)	476,652
Retained earnings:		
Designated	143,729	143,729
Undesignated	8,602,194	8,160,761
Total members' equity	12,300,899	13,418,382
Total liabilities and members' equity	\$ 37,011,705	\$ 30,741,407
<i>The accompanying notes are an integral part of these financial statements.</i>		

	1999	1998
Revenues:		
Premiums earned	\$ 15,411,073	\$12,661,968
Ceded premiums earned	(1,729,769)	(28,296)
Net premiums earned	13,681,304	12,633,672
Investment income (net of expenses of \$63,939 and \$31,527 in 1999 and 1998)	1,546,010	1,431,192
Net realized investment gains (losses)	31,119	(69,721)
Other	3,662	5,409
Total revenues	15,262,095	14,000,552
Expenses:		
Losses and loss adjustment expenses	11,392,539	11,233,527
Salaries and other compensation	1,739,046	1,430,178
General and administrative	788,013	861,606
Contracted services/professional fees	620,200	501,265
Risk control	280,864	182,495
Total expenses	14,820,662	14,209,071
Income (loss) before underwriting experience dividend	441,433	(208,519)
Reversal of prior year's underwriting experience dividend	—	121,823
Net income (loss)	\$ 441,433	\$ (86,696)
<i>The accompanying notes are an integral part of these financial statements.</i>		

	Members' Contributions	Accumulated Other Comprehensive Income	Retained Earnings		Total
			Designated	Undesignated	
Balance at December 31, 1997	\$ 4,495,283	\$ (142,667)	\$143,729	\$ 8,247,457	\$ 12,743,802
Comprehensive income:					
Net loss	—	—	—	(86,696)	(86,696)
Unrealized holding gains	—	549,598	—	—	549,598
Add: reclassification adjustment for losses included in net income	—	69,721	—	—	69,721
Other comprehensive income	—	619,319	—	—	619,319
Comprehensive income	—	—	—	—	532,623
Members' contributions, net	141,957	—	—	—	141,957
Balance at December 31, 1998	4,637,240	476,652	143,729	8,160,761	13,418,382
Comprehensive loss:					
Net income	—	—	—	441,433	441,433
Unrealized holding losses	—	(1,506,272)	—	—	(1,506,272)
Less: reclassification adjustment for gains included in net income	—	(31,119)	—	—	(31,119)
Other comprehensive loss	—	(1,537,391)	—	—	(1,537,391)
Comprehensive loss	—	—	—	—	(1,095,958)
Member withdrawals	(25,020)	—	—	—	(25,020)
Members' contributions, net	3,495	—	—	—	3,495
Balance at December 31, 1999	\$ 4,615,715	\$ (1,060,739)	\$143,729	\$ 8,602,194	\$ 12,300,899
<i>The accompanying notes are an integral part of these financial statements.</i>					

	1999	1998
Cash flows from operating activities:		
Net income (loss)	\$ 441,433	\$ (86,696)
Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities:		
Net realized investment (gain) losses	(31,119)	69,721
Gain on investment in HIG	—	(125,722)
Amortization and accretion on investments, net	(18,152)	796
Changes in assets and liabilities:		
Premiums receivable	(3,633,099)	1,044,436
Reinsurance escrow accounts	97,683	(868,796)
Reinsurance recoverable	(1,348,476)	—
Accrued investment income	(51,857)	(45,474)
Other assets	(684,136)	167,689
Due from affiliates	(4,900,000)	2,854,966
Unpaid losses and loss adjustment expenses	4,639,242	768,871
Unearned premiums	1,550,881	(657,848)
Reinsurance payable	1,277,732	—
Accrued expenses and other liabilities	(411,006)	74,629
Due to affiliates	330,932	34,607
Net cash (used in) provided by operating activities	(2,739,942)	3,231,179
Cash flows from investing activities:		
Purchases of available for sale securities	(7,871,262)	(15,568,745)
Investment in HIG	—	(95,359)
Proceeds from investments sold or matured	4,917,893	12,521,860
Investment repayments	960,200	1,477,494
Net cash used in investing activities	(1,993,169)	(1,664,750)
Cash flows from financing activities:		
Members' withdrawals	(25,020)	—
Members' contributions	3,495	141,957
Net cash (used in) provided by financing activities	(21,525)	141,957
Net (decrease) increase in cash	(4,754,636)	1,708,386
Cash and cash equivalents, beginning of year	6,482,894	4,774,508
Cash and cash equivalents, end of year	\$ 1,728,258	\$ 6,482,894
<i>The accompanying notes are an integral part of these financial statements.</i>		

NOTE 1 GENERAL

Reporting Entity — Housing Authority Property Insurance, Inc. (the Company or HAPI), was incorporated on August 11, 1988, under the laws of the State of Vermont. The Company is an association captive insurance company and was formed for the purpose of providing property insurance coverage to member public housing authorities (member PHAs) throughout the United States.

Concentrations — The Company provides property and workers' compensation insurance to member PHAs which are governed and funded by the U.S. Department of Housing and Urban Development. Certain changes in public policy and/or funding of member PHAs could have a significant impact on the operations of the Company.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments — The Company accounts for investments in accordance with Statement of Financial Accounting Standards No. 115 (FAS 115), *"Accounting for Certain Investments in Debt and Equity Securities."* The Company's management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. At December 31, 1999 and 1998, all of the Company's investments are classified as available for sale and are carried at fair value. Unrealized gains and losses relating to available for sale securities are reported as a separate component of members' equity as accumulated other comprehensive income. Realized investment gains and losses are determined on a specific identification basis.

The amortized costs of fixed maturities are adjusted for amortization of premiums and accretion of discounts. Such amortization and accretion are included in interest income.

Within the mortgage-backed securities portfolios, the Company invests in collateralized mortgage obligations and mortgage backed security pools. Each security carries a varying degree of prepayment and interest risk, which can impact the fair value and the ultimate amount of investment income earned. Acceleration or deceleration of prepayments of the underlying mortgages can be caused by interest rate changes.

The fair values of investments are measured using quoted market prices or dealer quotations, when available. When quoted market prices are not available, fair value is measured using quoted market prices for similar securities.

The investment in Housing Investment Group, Inc. (HIG) is accounted for under the equity method of accounting (see Note 5).

Cash and Cash Equivalents — For financial statement purposes, the Company considers all short-term investments with an original maturity of three months or less to be cash equivalents. For these short-term investments, the carrying amount is an estimate of market value. Additionally, HAPI maintains cash balances at several banks. Accounts at each institution are insured by the Federal Deposit Insurance Corporation up to \$100,000.

Policy Acquisition Costs — Policy acquisition costs, which consist of premium taxes, are expensed as incurred.

Unpaid Losses and Loss Adjustment Expenses Reserves — Unpaid losses and loss adjustment expense reserves represent estimated provisions for both reported and unreported claims incurred and related expenses. Because of the relatively short history of the Company's operations in workers' compensation and the limited population of insureds, the actual loss experience for workers' compensation may vary from the estimates carried on the balance sheets due to the inherent variability of losses. In determining unpaid losses and loss adjustment expense reserves, the Company annually reviews its overall position, its reserving techniques and its reinsurance. These reserves represent the estimated ultimate cost of all incurred claims and claim adjustment expenses. Since the reserves are based upon estimates, the ultimate liability may be more or less than such reserves. The effects of changes in such estimated reserves are included in the results of operations in the period in which the estimates are changed. Such changes may be material to the results of operations and could occur in a future period.

Revenue Recognition — Premiums are generally recognized as revenue on a pro rata basis over the policy term. The portion of premiums that will be earned in the future is deferred and reported as unearned premiums.

Reinsurance — In the normal course of business, the Company seeks to reduce losses by reinsuring certain levels of risk with reinsurers. Amounts recoverable from reinsurers are estimated in a manner consistent with the reinsurance contracts.

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

Fair Values of Financial Instruments — The Company values financial instruments as required by Financial Accounting Standards Board Statement 107, *"Disclosure about Fair Value of Financial Instruments."* The carrying amounts of cash, premiums receivable, amounts due from affiliates, accounts payable and accrued expenses approximate fair value.

Reclassifications — Certain reclassifications to the 1998 financial statements have been made in order to conform with the 1999 presentation. Such reclassifications did not have a material effect on the financial statements.

Comprehensive Income — During 1998, the Company adopted Financial Accounting Standards Board Statement 130, *"Reporting Comprehensive Income."* Comprehensive income is a measurement of certain changes in members' equity that result from transactions and other economic events other than transactions with members. For the Company, these consist of changes in unrealized gains and losses on the investment portfolio, which are used to adjust net income to arrive at comprehensive income. The cumulative amount of these changes is reported in the balance sheets within accumulated other comprehensive income.

NOTE 3 INVESTMENTS

Fixed maturities classified as available for sale and carried at fair value as of December 31, 1999, are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	\$ 1,285,902	\$ —	\$ (39,977)	\$ 1,245,925
State and political subdivisions	2,920,742	—	(140,982)	2,779,760
Corporate securities	7,074,154	654	(389,018)	6,685,790
Mortgage-backed securities	9,122,631	28	(448,856)	8,673,803
Foreign government bonds	502,038	—	(42,588)	459,450
Total available for sale	\$20,905,467	\$ 682	\$ (1,061,421)	\$ 19,844,728

Fixed maturities classified as available for sale and carried at fair value as of December 31, 1998, are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	\$ 2,849,834	\$ 118,795	\$ (1,750)	\$ 2,966,879
State and political subdivisions	2,456,511	81,644	—	2,538,155
Corporate securities	7,638,070	234,565	—	7,872,635
Mortgage-backed securities	5,918,612	52,953	(9,555)	5,962,010
Total available for sale	\$18,863,027	\$ 487,957	\$ (11,305)	\$ 19,339,679

The cost and fair value of fixed maturities are shown by contractual maturity as of December 31, 1999. 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.

	Amortized Cost	Fair Value
Due to mature:		
One year or less	\$ 649,910	\$ 649,776
After one year through five years	2,551,785	2,477,828
After five years through ten years	7,045,552	6,599,292
After ten years	1,535,589	1,444,029
Mortgage-backed securities	9,122,631	8,673,803
Total	\$ 20,905,467	\$19,844,728

Proceeds from sales and repayments of securities classified as available for sale amounted to \$5,878,093 and \$13,999,354 in 1999 and 1998, respectively. Gross gains of \$36,816 and \$142,227, and gross losses of \$5,697 and \$211,948 were realized on those sales during 1999 and 1998, respectively.

NOTE 4 INCOME TAXES

The Company has received a determination letter from the Internal Revenue Service indicating that the Company qualifies under the provisions of Section 115 of the Internal Revenue Code and is exempt from federal income taxes.

NOTE 5 RELATED PARTY TRANSACTIONS

In June 1995, the Company and Housing Authority Risk Retention Group, Inc. (HARRG) formed Housing Investment Group, Inc. (HIG) to serve as a for-profit holding company to govern the related businesses to which the Company and HARRG have an ownership interest. HIG has two classes of stock, a voting class (Class A) which is owned 50% by the Company and 50% by HARRG, and a non-voting class (Class B) which was initially owned 25% (3,000 shares Class B stock) by the Company and 75% (9,000 shares Class B stock) by HARRG. The ownership of the non-voting shares fluctuates based upon the relative capital bases of the Company and HARRG. The investment in HIG is accounted for under the equity method of accounting. At December 31, 1999 and 1998, the Company owned 26% and 25% (3,140 and 3,000 shares Class B stock) and HARRG owned 74% and 75% (8,860 and 9,000 shares of Class B stock), respectively.

The Company has an insurance services and cost-sharing agreement with HARRG, in which HARRG provides insurance management, underwriting, claims handling, property loss control, engineering and property valuation services on a fee-for-service basis. The actual costs of these services are being directly allocated to the Company. Total expenses amounted to approximately \$2,690,000 and \$2,350,000 for the years ended December 31, 1999 and 1998, respectively. The amounts due to HARRG, which are included in due to affiliates, were approximately \$566,000 and \$579,000 at December 31, 1999 and 1998, respectively.

The Company contracts with HAI to provide marketing services on behalf of HAPI. HAPI recognized expenses for these services of approximately \$80,600 and \$97,500 in 1999 and 1998, respectively.

In 1999, the Company advanced funds to HIS which were utilized to make claim payments to insureds. The amounts, which are included in due from affiliates, amounted to \$5,507,322.

The Company entered into an agreement with HTI to support the delivery of risk management training to members. The Company recognized an expense of \$157,992 and \$90,000 for fees paid to HTI for the years ended December 31, 1999 and 1998, respectively.

NOTE 6 MEMBERS' EQUITY

The Company is owned by its members and each member makes an initial capital contribution upon membership. The membership agreement requires each member to remain a member for a minimum of three years. If a member withdraws prior to the three-year period, the member forfeits its initial surplus contribution and any additional surplus contributions. If a member withdraws subsequent to the three-year period, other than as a result of certain specified events, it may either (1) withdraw its initial and any additional surplus contributions as defined by the membership agreement with such withdrawal to be completed at the discretion of the Board of Directors but not later than five years from the date of notice of withdrawal, or (2) maintain its surplus account with the Company, in which case it shall share in all allocations to and from surplus accounts as if it continued to be a member. Distributions can be at the earliest of the following three circumstances: (1) the close of all claims from the policy years in which the member participated, (2) the discretion of the Board of Directors, or (3) in the event of the liquidation of the Company.

As an association captive insurance company, HAPI is required by the Vermont Department of Banking, Insurance, Securities and Health Care Administration to maintain a minimum statutory surplus of \$750,000.

During 1999 and 1998, there were member PHAs that had withdrawn their membership in the Company, however, they have not formally requested a distribution of their surplus accounts. Should these members request a distribution of their surplus accounts, the Company will return the amount in accordance with the provisions of the membership agreement and the policy on member withdrawal as described above, and will classify the amounts as a liability within the balance sheet. During 1999, one member requested a distribution, which amounted to \$25,020 and is classified within accrued expenses and other liabilities.

The Company provides its members with underwriting experience dividends, which are calculated based upon the underwriting experience of each member and the 50% capital contribution, and are reflected as underwriting experience dividends in the statement of operations. There were no underwriting experience dividends accrued for in 1999 and 1998. In 1998, the Company reversed \$121,823 of accrued underwriting experience dividends due to PHAs that withdrew membership in the Company in 1998 or recorded underwriting losses and thereby disqualified themselves from receiving underwriting experience dividends.

The Company's Board of Directors designated retained earnings of \$143,729 in 1992 for the acquisition of land and construction of a building to be used for HARRG and the Company's offices.

NOTE 7 STATUTORY ACCOUNTING PRACTICES

The Vermont Department of Banking, Insurance, Securities and Health Care Administration (the Department) recognizes as net income and members' equity those amounts determined in conformity with statutory accounting practices prescribed or permitted by the Department, which differ in certain respects from generally accepted accounting principles. The amounts of statutory net (loss) earnings were approximately \$441,000 and \$(87,000) for the years ended December 31, 1999 and 1998, respectively. The amounts of statutory surplus were approximately \$12,770,000 and \$12,600,000 as of December 31, 1999 and 1998, respectively. Pursuant to the laws of the State of Vermont, the Company's dividend payments are limited to the lesser of 10% of statutory surplus or net income excluding realized capital gains.

In 1998, the National Association of Insurance Commissioners (NAIC) adopted the Codification of Statutory Accounting Principles guidance, which will replace the current Accounting Practices and Procedures manual as the NAIC's primary guidance on statutory accounting. The NAIC has recommended an effective date of January 1, 2001. The Company has not estimated the potential effect of the Codification guidance if adopted by the Vermont Department of Banking, Insurance, Securities and Health Care Administration.

NOTE 8 INSURANCE ACTIVITY

Premiums for property coverages were written and assumed primarily through fronting agreements. The Company assumes the first \$100,000 of loss and shares in 35% of the losses in the \$100,000 to \$1,000,000 layer. The Company also has aggregate coverage for losses within the Company's retention in excess of \$5,000,000 per catastrophic event. The Company has entered into a property aggregate stop-loss cover that limits its liability to 50% of gross earned premium up to \$1,000,000. This aggregate stop-loss cover is to be computed prior to the subsequent two stop-loss agreements.

The Company also assumes workers' compensation coverage in which the Company retains the first \$100,000 of losses subsequent to January 1, 1999. Prior to January 1, 1999, the Company's retention was \$250,000. The Company has a trust agreement and is required to maintain an escrow account for this program, which is reflected in the accompanying balance sheet. These funds are restricted in that they can only be used to pay for losses of the workers' compensation program.

In 1999, the Company reinsured HARRG under an aggregate excess of loss reinsurance agreement. The agreement provides for reinsurance protection to HARRG for all losses in excess of HARRG's retention, which was \$7,400,000 for the period July 1, 1999 to December 31, 1999. The agreement also provides for an individual coverage period and overall aggregate limit, which was \$3,300,000. The agreement provides for the deferral of payment of a portion of the reinsurance premium which amounted to \$1,803,255 at December 31, 1999, which is included in premiums receivable on the balance sheet. The Company also has recorded a ceding commission expense of \$346,823 and losses payable of \$973,409 for the year ending December 31, 1999.

In connection with the aforementioned treaty with HARRG, the Company entered into an aggregate excess of loss reinsurance agreement for the period July 1, 1999 to December 31, 2002. The agreement provides for reinsurance protection for all losses in excess of the Company's retention, which was \$5,500,000 for the period July 1, 1999 to December 31, 1999. The agreement also provides for an individual coverage period and overall aggregate limit, which was \$3,000,000. The agreement provides for the deferral of payment of a portion of the reinsurance premium which was \$1,652,732 for the year ending December 31, 1999. The Company also has recorded ceding commission income of \$357,798 and a reinsurance recoverable of \$1,348,476 for the year ending December 31, 1999.

The Company provides fidelity coverage and assumes 25% of the policy limits in excess of a 10% retention of policy limits up to maximum net retained liability of \$50,000. The Company also provides boiler and machinery coverages and assumes 10% of the policy limits up to maximum net retained liability of \$50,000.

The Company assumes 100% of auto physical damage coverages.

Premiums written, assumed and related reinsurance amounts for the years ended December 31, 1999 and 1998, are summarized as follows:

	Premiums Written		Premiums Earned	
	1999	1998	1999	1998
Direct premiums	\$ 108,407	\$ 147,570	\$ 126,052	\$ 151,888
Premiums assumed				
from other companies	16,902,967	11,856,551	15,285,021	12,510,080
Premiums ceded				
to other companies	(1,779,188)	(12,657)	(1,729,769)	(28,296)
Net premiums	\$15,232,186	\$ 11,991,464	\$13,681,304	\$12,633,672

The Company recorded reinsurance recoveries of \$1,348,476 in 1999, which is reflected as a reduction in losses and loss expenses incurred in the Statements of Operations.

A reconciliation of changes in unpaid losses and loss adjustment expenses for the years ended December 31, 1999 and 1998, are summarized as follows (in thousands):		
	1999	1998
Balance at beginning of year	\$11,193	\$ 10,424
Incurred related to:		
Current year	9,580	9,807
Prior years	912	1,451
Total incurred	10,492	11,258
Paid related to:		
Current year	(2,768)	(4,032)
Prior years	(4,434)	(6,457)
Total paid	(7,202)	(10,489)
Net balance at end of year	14,483	11,193
Plus reinsurance recoverable	1,349	—
Balance at end of year	\$15,832	\$ 11,193
As a result of changes in loss development, the provision of claims and claim adjustment expenses increased by \$912,000 and \$1,451,000 in 1999 and 1998, respectively. The loss development trend is within the normal range for the industry.		
NOTE 9 COMMITMENTS AND CONTINGENCIES		
In December 1996, the Company and HARRG approved the issuance of a \$771,000 line of credit to HTI. To date, no amounts have been drawn with HAPI.		

Management's Discussion and Analysis

For the years ended December 31, 1999 and 1998

THE COMPANY - AN OVERVIEW

Housing Authority Property Insurance, Inc. (The Company or HAPI), was incorporated on August 11, 1988, as a mutual captive insurer. HAPI provides property and casualty insurance to member housing authorities throughout the United States. HAPI is a nonprofit, federal tax-exempt company owned by member public housing authorities (PHAs). HAPI was developed as a result of the inability of many PHAs to obtain comprehensive property coverage at reasonable rates. Effective December 31, 1998, HAPI converted its charter in the State of Vermont back to a mutual captive insurer, a reversion from its mutual domestic insurer status established in 1996.

HAPI is a niche market insurer. The Company only serves PHAs in the United States. Currently, HAPI underwrites 26% of this market on a per unit basis. HAPI's Board of Directors and various committees review the mission and vision statement of the Company at their quarterly meetings and meet annually to update these statements.

HAPI premiums for property coverages were written and assumed primarily through fronting agreements. The Company's property program assumes the first \$100,000 of loss and shares in 35% of the losses in the \$100,000 to \$1,000,000 layer. The Company has entered into a property aggregate stop-loss cover that limits its liability to 50% of gross earned premium up to \$1,000,000.

The Company also assumes workers' compensation coverage in which the Company retains the first \$100,000 of losses subsequent to January 1, 1999. Prior to January 1, 1999, the Company's retention was \$250,000. The Company has a trust agreement and is required to maintain an escrow account for this program. These funds are restricted in that they can only be used to pay for losses of the workers' compensation program.

In 1999, the Company reinsured HARRG under an aggregate excess of loss reinsurance agreement. The agreement provides for reinsurance protection to HARRG for all losses in excess of HARRG's defined retention. The contract does provide for coverage period and cumulative limits. This contract is effective through December 31, 2002. In connection with this treaty with HARRG, the Company entered into an aggregate excess of loss reinsurance agreement with a third-party reinsurer. This contract is also effective through December 31, 2002.

HAPI provides a significant amount of property insurance to housing authorities. In 1996, HAPI hired an actuarial firm to perform a wind catastrophic study that would determine the loss severity potential of the Company. The result of the study projected a maximum loss potential of about \$1.2 million using a 100-year probability event assumption. During that year, the Company reduced its wind potential by purchasing aggregate stop loss coverage and adding windstorm sublimits to various policies that have an exposure. In 1998, a member of HAPI with a large property schedule with coastal wind exposure non-renewed their policy. In addition, aggregate reinsurance coverage was obtained for losses within the retention in excess of \$5,000,000 per catastrophe. These changes have reduced the wind catastrophe exposure.

In June 1995, HAPI and Housing Authority Risk Retention Group, Inc. (HARRG) formed Housing Investment Group, Inc. (HIG) to serve as a for-profit holding company to govern related businesses to which the Company and HARRG have an ownership interest. With the incorporation of HIG, the Company and

HARRG consolidated all of the for-profit business entities under the holding company effective January 1, 1996. The subsidiaries include: Housing Insurance Services, Inc. (HIS) (insurance agency), Housing Environmental Services, Inc. (HES) (environmental testing laboratory), and Satellite Telecommunications, Inc. (STI) (satellite telecommunications services).

The following discussion provides an assessment by management of the current GAAP financial position, results of operations, cash flow and liquidity, and changes in financial position for HAPI. Information presented in this discussion supplements the financial statements, schedules, and exhibits of the 1999 GAAP Audited Financial Statements.

1999 ENVIRONMENT

The U.S. property/casualty market continued to show weak premium growth due to heavy premium price discounting and new competition due to the availability of low cost capital. Industry profits in 1999 are projected to show a second year of decline from the record profits recorded by the industry in 1997. The combined ratio is estimated at 108.0% versus 105.6% for 1998 primarily due to the heavy premium discounting and poor workers' compensation results. Reinsurance pricing is beginning to show some signs of modest firming, but dramatic changes in the primary markets are not anticipated until there is a significant depletion of capital.

FINANCIAL POSITION

HAPI's total assets at year-end 1999 were \$37,011,705, an increase of \$6,270,298 or 20.4% from 1998 assets of \$30,741,407. This growth was due in large part to premium receivables and increased investments reflecting positive cash flows from the addition of 80 new members in 1999 and the retention of 98% of current members.

Cash on hand at year-end 1998 and cash flows from investment income were directed into the investment portfolio and invested in mortgage-backed securities and investment grade corporate bonds. The investment portfolio, on an amortized cost basis, increased by \$2,042,440 or 10.8%, to \$20,905,467 at December 31, 1999, versus \$18,863,027 at December 31, 1998. The investment portfolio, at fair market value, was \$19,844,728 as of December 31, 1999, up only slightly due to a \$1,537,391 unrealized loss.

Funds deposited with reinsurance companies in escrow accounts at \$2,232,261 as of December 31, 1999, were essentially unchanged from 1998. Amounts due from affiliates as of December 31, 1999, increased to \$5,507,322 from \$607,322 at December 31, 1998. This increase reflects receivables for premiums and paid loss reimbursements.

Reserves for unpaid losses and loss adjustment expenses at December 31, 1999, reflect the estimate of the liability for the ultimate net cost of reported claims and estimated "incurred but not reported" (IBNR) claims arising from losses which occurred by year's end. The Company has retained an independent actuarial consulting firm to determine the adequacy of reserves on an annual basis. At December 31, 1999, reserves for unpaid losses and loss adjustment expenses, including IBNR reserves, were \$15,832,150, an increase of \$4,639,242 or 41.4% over the 1998 figure of \$11,192,908. This increase is due to growth in workers' compensation, poor experience on one large workers' compensation account, and strengthening of the IBNR reserve levels. Loss and loss adjustment expense reserves are not discounted. Salvage and subrogation recoveries are not considered when setting reserves.

Unearned premiums increased to \$5,683,674 at December 31, 1999, from \$4,132,793 at December 31, 1998. This tracks the growth in written premium.

Accrued expenses decreased to \$996,157 at December 31, 1999, from \$1,407,163 at December 31, 1998. This decrease is primarily due to settlement of the employee lawsuit discussed later.

In 1997, the Company accrued underwriting experience dividends of \$500,000. A portion of this accrual was not needed and \$121,823 was included in 1998 net income. No similar accrual was recorded either in 1998 or 1999.

Capital and surplus decreased by \$1,117,483 or 8.3% to \$12,300,899 versus the prior year's balance of \$13,418,382. This reflects an unrealized investment loss of \$1,537,391 partially offset by net income of \$441,433.

RESULTS OF OPERATIONS

Net premiums written for 1999 were up by 27.1% to \$15,236,429 from \$11,991,464 in 1998. This increase is attributable to the addition of 53 new property members and 27 new workers' compensation members, and 98% retention of existing members. Earned premiums increased by \$1,047,632 or 8.3% to \$13,681,304 for the year ended December 31, 1999, versus \$12,633,672 for the same period in 1998.

Investment income for the year ended December 31, 1999, was \$1,546,010, an increase of \$114,818 or 8.0% above 1998 income of \$1,431,192. Investment income was positively impacted by growth in the investment portfolio. Gains from the sale of securities aggregated \$31,119 for the year ended December 31, 1999, versus the \$69,721 loss recorded in 1998.

In the beginning of 1998, the investment portfolio was managed both internally and by an external manager. In March of 1998, the decision was made to move the remaining in-house portfolio and all externally managed funds to Wellington Management Company. Investment policy calls for the portfolio to be managed on a "total rate of return" basis. This concept breaks returns down into two components: coupon yield and capital appreciation. As a result, realized and unrealized gains or losses from securities' transactions are a component of HAPI's investment return.

Loss and loss adjustment expenses incurred totaled \$11,392,539 for the year ended December 31, 1999, essentially unchanged from the \$11,233,527 recorded for the same period in 1998. Management modified its reinsurance agreements to reduce its workers' compensation exposure beginning in 1999. The loss ratio improved from 88.9% in 1998 to 83.3% in 1999. An annual claims audit was performed by an independent consulting firm and the results confirmed that the Company was handling claims in an efficient and professional manner. As part of this audit process, claims reserving practices are reviewed in order to ascertain that ultimate values are being set on claims.

The Company has an insurance services and cost-sharing agreement with HARRG, in which HARRG provides insurance management, underwriting, claims handling, property loss control, engineering and property valuation services on a fee-for-service basis. The actual costs of these services are being allocated to the Company. Total expenses amounted to approximately \$2,690,000 and \$2,350,000 for the years ended December 31, 1999 and 1998, respectively.

Operating expenses (which include the above service charges) increased to \$3,428,123 up 15.2% for the year ended December 31, 1999, from \$2,975,544 for the same period in 1998. HAPI's expense ratio has increased from 23.6% in 1998 to 25.1% in 1999. This reflects higher staff and systems expenses associated with business growth.

HAPI had a net income of \$441,433 for 1999 versus a loss of \$86,696 for the same period in 1998. The improvement for the most part is due to favorable results on an aggregate stop loss contract with HARRG. Management is continually seeking ways to enhance operating performance.

In 1999, the Company settled a lawsuit brought by a former employee alleging breach of contract under the terms of an employment agreement which expired on July 13, 1999. The final settlement, which relieves the Company of all future liabilities, was within the amount accrued as part of the 1998 financial statements.

CASH FLOW AND LIQUIDITY

Liquidity can be defined as the Company's ability to generate sufficient cash flows to meet the cash requirements of operations, primarily paying losses and other underwriting expenses. Primary sources of cash include cash flow from operations, i.e., premium and investment income, cash provided from the sale or maturity of invested assets, and capital contributions from members. The Company generated net negative cash flow of \$2,739,942 from operations, due to timing differences in the collection of insurance premiums and payment of losses. Cash on hand decreased from \$6,482,894 at December 31, 1998 to \$1,728,258 at December 31, 1999.

HAPI currently has no borrowed funds.

MANAGEMENT INFORMATION SYSTEMS

Considerable time and expense (\$124,681) were directed at ensuring that hardware, custom and vendor software and third party interfaces would function in 2000. The changeover occurred without interruption to business processes.

Management believes that the effective use of technology is critical to the success of the organization as the market becomes increasingly competitive. The Company has implemented several customized systems that include Underwriting (rating/quoting, policy issuance), Claims (payments, reserve tracking, and loss reporting), Administration (customer information) and Report Writer (financial reporting). The accounting system has been tightly integrated with the customized systems. Work is also progressing in connection with the expanded use of the Internet for the purpose of communicating and sharing information with the Company's policyholders and vendors. Nearly \$262,198 was expended in 1999 for systems' development.

BOARD POLICES AND MANAGEMENT PRACTICES

The Board of Directors of the Company currently requires that audits, conducted by independent outside firms, be performed on an annual basis. The 1999 audit schedule included: (1) an actuarial loss certification, submitted as part of the 1999 Annual Statement; (2) a claims audit performed in October 1999; (3) a financial audit for both GAAP and SAP, which will be completed by the end of May 2000; (4) an investment review of performance, conducted on a quarterly basis; and (5) an underwriting audit, conducted by the Company's reinsurers prior to December 31, 1999.

The Company's policy objective is to break even for underwriting. In 1999, a combined ratio of 108.3% was recorded. The two-year overall combined ratio was 110.3%. The operating ratio for the same two-year period, which includes investment results and other income, was 99.2%.

OPINION

The preceding Management's Discussion and Analysis provides an assessment of the financial position, results of operations, and cash flow and liquidity for the fiscal year ended December 31, 1999, as reported in the 1999 GAAP Audited Financial Statements. Representations made herein are those of management according to the best of their knowledge and belief.

Dated: March 31, 2000

/s/ **Daniel Labrie**

President and Chief Executive Officer

/s/ **Carol Pollack**

CFO & Treasurer

*Continued from
inside front cover*

Easton, MD	St. Louis, MO	Old Bridge, NJ	Monticello, NY	Temple, OK	McAllen, TX
Frederick, MD	Hattiesburg, MS	Orange, NJ	Mount Kisco, NY	Tuttle, OK	Mercedes, TX
Frostburg, MD	Asheboro, NC	Passaic, NJ	New Rochelle, NY	Walters, OK	Pharr, TX
Glen Burnie, MD	Durham, NC	Paterson, NJ	Newark, NY	Waynoka, OK	San Antonio, TX
Glenarden, MD	Fayetteville, NC	Penns Grove, NJ	Niagara Falls, NY	Weleetka, OK	San Benito, TX
Havre De Grace, MD	High Point, NC	Perth Amboy, NJ	Olean, NY	Wewoka, OK	Sherman, TX
Largo, MD	Kinston, NC	Phillipsburg, NJ	Plattsburgh, NY	Boswell, PA	Taylor, TX
Leonardtown, MD	Mid-East Regional, NC	Pleasantville, NJ	Port Chester, NY	Bradford, PA	Temple, TX
Saint Michael's, MD	Raleigh, NC	Red Bank, NJ	Port Jervis, NY	Dunmore, PA	Three Rivers, TX
Auburn, ME	Randleman, NC	Salem, NJ	Poughkeepsie, NY	Franklin, PA	Vera Cruz, TX
Bath, ME	Smithfield, NC	Trenton, NJ	Rensselaer, NY	Harrisburg, PA	Price, UT
Biddeford, ME	Tarboro, NC	Union City, NJ	Rochester, NY	Hollidaysburg, PA	Alexandria, VA
Brewer, ME	Washington, NC	Vineland, NJ	Rockville Centre, NY	Norristown, PA	Bristol, VA
Lewiston, ME	Cozad, NE	Wildwood, NJ	Spring Valley, NY	Philadelphia, PA	Charlottesville, VA
Old Town, ME	Crete, NE	Alamogordo, NM	Suffern, NY	Pittsburgh, PA	Coeburn, VA
Portland, ME	Lincoln, NE	Artesia, NM	Syracuse, NY	Punxsutawney, PA	Danville, VA
Bay City, MI	Niobrara, NE	Bayard, NM	Troy, NY	Reading, PA	Fairfax, VA
Benton Harbor, MI	Omaha, NE	Bernalillo, NM	Watertown, NY	Scranton, PA	Franklin, VA
Benton Township, MI	Tilden, NE	Clovis, NM	White Plains, NY	Stroudsburg, PA	Hopewell, VA
Clinton Township, MI	Verdigre, NE	Espanola, NM	Woodridge, NY	Titusville, PA	Jonesville, VA
Curtis, MI	Berlin, NH	Eunice, NM	Yonkers, NY	Warren, PA	Lebanon, VA
Detroit, MI	Claremont, NH	Fort Sumner, NM	Akron, OH	Central Falls, RI	Newport News, VA
Ecorse, MI	Derry, NH	Lovington, NM	Ashtabula, OH	Cranston, RI	Norfolk, VA
Essexville, MI	Exeter, NH	Raton, NM	Bidwell, OH	Cumberland, RI	Norton, VA
Flint, MI	Franklin, NH	Rio Arriba County, NM	Cambridge, OH	East Providence, RI	Petersburg, VA
Gladwin, MI	Keene, NH	Santa Clara, NM	Canton, OH	Greenville, RI	Portsmouth, VA
Grand Rapids, MI	Lancaster, NH	Santa Fe, NM	Chillicothe, OH	Harrisville, RI	Richmond, VA
Hamtramck, MI	Flint, MI	Santa Fe County, NM	Cincinnati, OH	Jamestown, RI	Roanoke, VA
Inkster, MI	Gladwin, MI	Socorro, NM	Cleveland, OH	Lincoln, RI	Waynesboro, VA
Landover, MI	Grand Rapids, MI	Springer, NM	Columbus, OH	Newport, RI	Williamsburg, VA
Lansing, MI	Hamtramck, MI	Truth or Consequence, NM	East Liverpool, OH	North Providence, RI	Barre, VT
Livonia, MI	Inkster, MI	Clark County, NV	Lorain, OH	Pawtucket, RI	Rutland, VT
Manistee, MI	Landover, MI	Las Vegas, NV	Manchester, OH	Peace Dale, RI	Springfield, VT
Muskegon, MI	Lansing, MI	Albany, NY	McConnellsville, OH	Portsmouth, RI	White River Junction, VT
Muskegon Heights, MI	Livonia, MI	Amsterdam, NY	Mt. Auburn, OH	Providence, RI	Winooski, VT
Pontiac, MI	Manistee, MI	Auburn, NY	Ravenna, OH	Warwick, RI	Bremerton, WA
Reed City, MI	Muskegon, MI	Beacon, NY	Sandusky, OH	Westerly, RI	Moses Lake, WA
Saginaw, MI	Muskegon Heights, MI	Binghamton, NY	Steubenville, OH	Woonsocket, RI	Seattle, WA
Saint Clair Shores, MI	Pontiac, MI	Brasher Falls, NY	Toledo, OH	Florence, SC	Silverdale, WA
St. Joseph, MI	Reed City, MI	Buffalo, NY	Zanesville, OH	Florence, SC	Tacoma, WA
Sterling Heights, MI	Saginaw, MI	Carthage, NY	Anadarko, OK	Marlboro, SC	Tacoma, WA
Ypsilanti, MI	Saint Clair Shores, MI	Catskill, NY	Antlers, OK	Mccoll, SC	Algoma, WI
Duluth, MN	St. Joseph, MI	Cortland, NY	Apache, OK	North Charleston, SC	Appleton, WI
Ely, MN	Sterling Heights, MI	Dunkirk, NY	Atoka, OK	Chattanooga, TN	Deforest, WI
Grand Rapids, MN	Ypsilanti, MI	Ellenville, NY	Cache, OK	Dyersburg, TN	Elkhorn, WI
Hopkins, MN	Duluth, MN	Elmira, NY	Comanche, OK	Knoxville, TN	Fond Du Lac, WI
Hutchinson, MN	Ely, MN	Freeport, NY	Del City, OK	Memphis, TN	Green Bay, WI
International Falls, MN	Grand Rapids, MN	Geneva, NY	Elk City, OK	Nashville, TN	Hudson, WI
Lake Benton, MN	Hopkins, MN	Glen Cove, NY	Fort Gibson, OK	Waverly, TN	Madison, WI
Minneapolis, MN	Hutchinson, MN	Glens Falls, NY	Geary, OK	Austin, TX	Milwaukee, WI
Moorhead, MN	International Falls, MN	Gloversville, NY	Guthrie, OK	Borger, TX	New Richmond, WI
Moose Lake, MN	Lake Benton, MN	Great Neck, NY	Haileyville, OK	Corpus Christi, TX	Racine, WI
Mound, MN	Minneapolis, MN	Greenburgh, NY	Hartshorne, OK	Dallas, TX	Rhineland, WI
Ortonville, MN	Moorhead, MN	Hempstead, NY	Holdenville, OK	Devine, TX	Superior, WI
South St. Paul, MN	Moose Lake, MN	Hornell, NY	Lawton, OK	El Campo, TX	Bluefield, WV
St. Paul, MN	Mound, MN	Hudson, NY	Mcalester, OK	El Paso, TX	Buckhannon, WV
Two Harbors, MN	Ortonville, MN	Ilion, NY	Miami, OK	Fort Worth, TX	Clarksburg, WV
Winona, MN	South St. Paul, MN	Ithaca, NY	Newkirk, OK	Galveston, TX	Fairmont, WV
Kansas City, MO	St. Paul, MN	Kingston, NY	Norman, OK	Garrison, TX	Huntington, WV
Saint Louis, MO	Two Harbors, MN	Lackawanna, NY	Oklahoma City, OK	Houston, TX	Saint Albans, WV
Smithville, MO	Winona, MN	Mamaroneck, NY	Ponca City, OK	Laredo, TX	Buffalo, WY
	Kansas City, MO	Massena, NY	Shawnee, OK	Liberty, TX	Casper, WY
	Saint Louis, MO	Mechanicville, NY	Stillwater, OK	Los Fresnos, TX	Casper, WY
	Smithville, MO		Stroud, OK	Maud, TX	Cheyenne, WY



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