



REPORT OF THE ANNUAL MEETING

April 22, 2005

WEST VIRGINIA ESSENTIAL PROPERTY INSURANCE ASSOCIATION

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

Board of Directors
2004-2005 Term

Mr. William Lingenfelter, Chairman	State Farm Insurance Companies
Mr. David A. McMillen, Vice Chairman.	Westfield Companies
Mr. Gary Auvil	Farmers Mutual Insurance Company
Mr. David V. Freeman	Erie Insurance Group
Mr. Thomas M. Giffen	Acordia of West Virginia
Ms. Michele Lilly	Nationwide Insurance
Mr. Jeffrey Williams, Esq.	Allstate Insurance Company
Mr. Samuel P. Gerace, Esq. General Counsel	Jones, Gregg, Creehan & Gerace, LLP
Mr. John M. Ogle, General Manager	West Virginia Essential Property Insurance Association

AGENDA
ANNUAL MEETING
OF THE
WEST VIRGINIA ESSENTIAL PROPERTY INSURANCE ASSOCIATION
APRIL 22, 2005
8:00 A. M.
EMBASSY SUITES - CHARLESTON, WEST VIRGINIA

1. Call to Order - 8:00 A.M. - William Lingenfelter, Chairman, presiding
2. Approval of Minutes of Annual Meeting - April 15, 2004
3. Ratification of Board Action
4. Report of Chairman
5. Report of General Manager
6. Treasurer's Report
7. Appointment of Board of Directors 2005 - 2006
(Appointment by Insurance Commissioner)
8. New Business
9. Adjournment

Minutes of the Annual Meeting
of the Board of Directors
of the West Virginia Essential Property Insurance Association
April 22, 2005
8:00 a.m.
Embassy Suites Hotel
Charleston, West Virginia

The West Virginia Essential Property Insurance Association Annual Meeting was held on April 22, 2005 at the Embassy Suites Hotel in Charleston, West Virginia. The Annual Meeting was called to order at 8:00 a.m. with Chairman William Lingenfelter presiding and Mr. John M. Ogle acting as secretary for the meeting.

Upon motion duly made, seconded and carried, the Minutes of the April 15, 2004 Annual Meeting were approved as distributed to member companies.

A motion to ratify the Board of Directors 2004-2005 term was duly made, seconded and carried.

Upon motion duly made, seconded and carried, the reading of the Chairman's Report, the General Manager's Report and the Treasurer's Report were waived as all three reports were included in the agenda packet and will be incorporated into the Annual Report made available to member companies.

Upon motion duly made, seconded and carried, the reports were accepted as presented.

By Notice of the West Virginia Insurance Commissioner, the Honorable Jane L. Cline, the following individuals were appointed to the Board of Directors of the West Virginia Essential Property Insurance Association for the 2005 - 2006 term.

Mr. Gary R. Auvil
Farmers Mutual Insurance Company

Mr. David V. Freeman
Erie Insurance Group

Mr. Thomas M. Giffen
Acordia

Mr. William Lingenfelter
State Farm Insurance Companies

Ms. Michele Lilly
Nationwide Insurance

Mr. David A. McMillen
Westfield Companies

Mr. Jeffrey Williams
Allstate Insurance Company

General Manager Ogle noted the 2004 Year End Financial Audit was not yet finalized and would be provided to the Board of Directors in the near future. The audit will be made part of the Annual Report distributed to member companies.

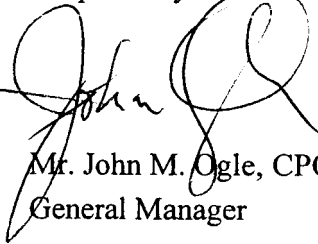
There being no further business and upon motion duly made, seconded and carried, the meeting was adjourned.

Approved by,



Mr. William Lingenfelter
Chairman of the Board

Respectfully submitted by



Mr. John M. Ogle, CPCU
General Manager

Chairman's Report
Chairman William Lingenfelter
West Virginia Essential Property Insurance Association
Annual Meeting of
the Board of Directors
April 22, 2005
Charleston, West Virginia - Embassy Suites Hotel
8:00 a.m.

Good Morning. Welcome to the 19th Annual Meeting of the West Virginia Essential Property Insurance Association.

As I look back over this past year, I cannot help but be reminded of the previous 18 years. Since our inception, the Association has issued 26,390 policies while collecting just under \$9.3 million in Written Premium and incurring slightly over \$7.7 million in losses. Although the Association has historically been a small, geographically concentrated organization, it has provided quality service to all areas of the state throughout its 18 year history. In addition, the West Virginia Essential Property Insurance Association has maintained a diligent stand against arson and fraud and continues to be the sole financial support for the West Virginia Arson Hotline Program.

Although the General Manager's Report will review the 2004 statistics, I would like to share with you our year-end financial results. In 2004, the Association recorded an Underwriting deficit of \$157,259. Taking into account Investment Income and Other Income and Expenses, the Net Result of Operations for 2004 was a deficit of \$159,103. New Business Received grew by just over 16% and Total Policies Issued increased by 18%. Although the Association remains small, the increased activity brings to light the important role the Association plays in the West Virginia marketplace. As local markets ebb and flow, the West Virginia Essential Property Insurance Association maintains its presence ready to meet the needs of the property owners.

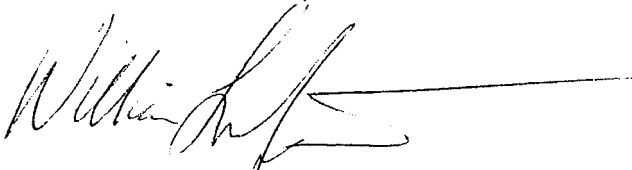
The Association provides the sole financial support to the West Virginia Arson Hotline Program. This year the dedicated and hardworking staff of the Fire Marshall's Office combined with the emergence of this well publicized Hotline produced several arson convictions and resulted in several thousand dollars of reward money. On behalf of the Board, our thanks goes out to the State Fire Marshall's Office investigators, to the Hotline Committee Members and in particular, Committee Chairman Michael Phelps.

The Association continues to operate with the vital assistance of the Insurance Placement Facility of Pennsylvania. Through this arrangement, wherein expenses and expertise are shared, the West Virginia Essential Property Insurance Association is able to maintain its small, but vital role in the West Virginia insurance industry. Special thanks are extended to General Manager John Ogle and his fine staff for their dedication to the West Virginia Essential Property Insurance Association.

Throughout the year, the organization experienced numerous changes to the Board and governing committees. To those individuals who have left us but given so freely of their time and expertise, I would like to express my gratitude for their efforts. It is clear the insurance industry is made up of many talented and professional individuals and this organization is fortunate to have many of those same people serving on our Board and Governing Committees.

In closing, I would like to express my thanks to General Counsel, Mr. Samuel Gerace for his timely and thorough legal advice. I would also like to recognize and thank the West Virginia State Insurance Department for their active participation and involvement. Lastly, I would like to take this opportunity to thank each of my fellow Board Members for their individual contributions to this organization. Your support has been gratifying and I am confident that the West Virginia Essential Property Insurance Association remains in capable hands.

Respectively submitted,

A handwritten signature in black ink, appearing to read "William Lingenfelter", with a long horizontal line extending to the right.

Mr. William Lingenfelter
Chairman of the Board of Directors

General Manager's Report
John M. Ogle
West Virginia Essential Property Insurance Association
Annual Meeting
April 22, 2005
Embassy Suites Hotel
Charleston, West Virginia
8:00 a.m.

Good Morning. I am pleased to be here with you this morning and to have this opportunity to share the highlights and results of this past year. In 2004, the West Virginia Essential Property Insurance Association issued 1,687 policies, an increase of 18.2% from 2003. The increase in Policies Issued was part of an ongoing trend first established in 2001. In 2004, New Applications Received increased 16.6% while Renewal Policies Issued increased 25.6% to 1,016. The increase in business increased Premiums Written by 18.8% to \$866,737 and Premiums Earned by 34.5% to \$809,479.

On the claims side, in 2004 the Association experienced a 110% increase in Losses Reported, from 20 to 42. The Association posted a Total Loss Incurred of \$536,561. The Average Paid Loss decreased 14% to \$15,753 and for the year, the Pure Loss Ratio rose slightly more than 20 points to 66.28%. The West Virginia Essential Property Insurance Association recorded no claim litigation activity during the year and unlike our very early years of operation, the Association currently has no outstanding files in litigation.

All in all, the Plan recorded a 2004 underwriting deficit of \$157,259 and a Net Result of Operations deficit of \$159,103.

This past year will be remembered for two items. The Association continued to grow by double digit percentages and by the end of the year more than doubled in Premiums Written. In 2001 the Association issued 956 policies, but by December 31, 2004, that number was 1,687. Secondly, 2004 will be remembered as the year of the large loss. The Association recorded only 16 fire losses but four were serious fire losses in excess of \$50,000. As such, both Loss Incurred and Loss Adjustment Expenses Incurred were negatively impacted.

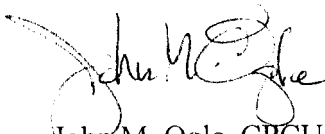
On a brighter note, the major storms that dominated the headlines throughout the 2004 hurricane season, had little impact on the Association. The West Virginia Essential Property Insurance Association was impacted by just one event, which yielded just one paid loss.

As we approach our 20th year of operation, the Association remains in a specter of uncertainty. As the insurance marketplace again adjusts itself to the changing conditions of the marketplace, the impact on the West Virginia Essential Property Insurance Association is unknown. Although the future remains cloudy, the Association is prepared to meet the challenges that lie ahead. The West Virginia Essential Property Insurance Association remains committed to operating a professional and efficient association to service the property insurance industry as well as the insurance buying public.

In closing, I would like to thank General Counsel Gerace and his staff for their tireless efforts and attention to detail in assisting the Plan throughout the year. I would also like to thank the West Virginia Insurance Department for their input and guidance throughout 2004.

The West Virginia Essential Property Insurance Association is fortunate to have the contribution of many talented Board and Committee Members. I would like to extend my gratitude to each individual for contributing their expertise, advice and most of all, their support. Lastly, I would like to thank the individual employees, management and staff alike, for their dedication and commitment to the association. It is because of their fine efforts that we can look back on a successful year and look forward to the challenges of the future.

Respectively,

A handwritten signature in black ink, appearing to read "John M. Ogle". The signature is stylized and cursive.

John M. Ogle, CPCU
General Manager

WEST VIRGINIA ESSENTIAL PROPERTY INSURANCE ASSOCIATION

WEST VIRGINIA FAIR PLAN

Treasurer's Report

December 31, 2004


ASSETS

Cash in Bank	884,897.81
Investments, Short term at cost plus accumulated discount	65,542.12
Accrued Investment Income	0.00
Due from Participating Members	0.00
Premiums Receivable	12,978.66
Other Receivables	0.00
Prepaid Premium Tax	0.00
Equipment	0.00
	<hr/>
Total Assets	<u>963,418.59</u>

LIABILITIES AND MEMBERS' EQUITY

Unearned Premiums	456,258.00
Unearned Advance Premiums	15,524.00
Outstanding Losses	299,500.00
Outstanding Loss Adjustment Expenses	66,169.00
Accrued Expenses	6,458.00
Unpaid Post Retirement Benefits	67,374.00
Accounts Payable	3,103.89
Claims Checks Payable	180,041.17
Unpaid Premium Tax	12,745.08
	<hr/>
Total Liabilities	1,107,173.14
Members' Equity (Deficit)	<u>(143,754.55)</u>
	<hr/>
Total Liabilities and Members' Equity	<u>963,418.59</u>

Respectfully Submitted,



RoseMarie McDonald
Accounting Manager



STATE OF WEST VIRGINIA


Offices of the Insurance Commissioner

JOE MANCHIN III
Governor

JANE L. CLINE
Insurance Commissioner

MEMORANDUM

TO: Thomas M. Giffen - Acordia of West Virginia
William Lingenfelter - State Farm Insurance Companies
David A. McMillen - Westfield Companies
David V. Freeman - Erie Insurance Group
Gary R. Auvil - Farmers' Mutual Insurance Company
Michele Lilly - Nationwide Insurance Company
Jeffrey Williams, Esq. - Allstate Insurance Company

FROM: 
Jane L. Cline
Insurance Commissioner

DATE: March 29, 2005

RE: **Board of Directors - 2005-06**
West Virginia Essential Property Insurance Association
FAIR PLAN

I hereby appoint the above Board of Directors of the West Virginia Essential Property Insurance Association for 2005-06. I look forward to our efforts in maintaining an effective FAIR Plan.

JLC/csp

cc: John M. Ogle, CPCU
General Manager



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

The Board of Directors
West Virginia Essential Property Insurance Association:

We have audited the accompanying statutory statements of admitted assets, liabilities, and members' (deficit) equity of West Virginia Essential Property Insurance Association (the Association) as of December 31, 2004 and 2003, and the related statutory statements of operations and members' (deficit) equity and cash flows for the years then ended. These statutory financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described more fully in note 1 to the statutory financial statements, the Association prepared these statutory financial statements using accounting practices prescribed or permitted by the Insurance Department of the State of West Virginia, which differ from accounting principles generally accepted in the United States of America. The effects on the statutory financial statements of the variances between the statutory basis of accounting and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

The Association's liabilities exceeded its assets by \$134,354 at December 31, 2004. Such an amount, however, is recoverable from member companies (note 2).

In our opinion, because of the effects of the matter discussed in the third paragraph, the statutory financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of West Virginia Essential Property Insurance Association as of December 31, 2004 and 2003, or the results of its operations or its cash flows for the years then ended.

Also, in our opinion, the statutory financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and members' (deficit) equity of West Virginia Essential Property Insurance Association as of December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in note 1.

As discussed in note 4, the Association changed the manner in which it account for its additional minimum pension liabilities in 2004 to conform to the requirements of SSAP No. 89, *Accounting for Pensions, A Replacement of SSAP No. 8*.

Our audits were made for the purpose of forming an opinion on the basic statutory financial statements taken as a whole. The supplementary information included on the supplemental investment risk interrogatories in schedule 1 and the summary of investments in schedule 2 is presented for purposes of additional analysis and is not a required part of the basic statutory financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic statutory financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic statutory financial statements taken as a whole.

KPMG LLP

March 25, 2005

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Statutory Statements of Admitted Assets, Liabilities, and Members' (Deficit) Equity

December 31, 2004 and 2003

Admitted Assets	<u>2004</u>	<u>2003</u>
Cash and cash equivalents, at cost which approximates market value	\$ 950,440	694,711
Premiums receivable	12,979	5,284
Total admitted assets	<u>\$ 963,419</u>	<u>699,995</u>
Liabilities and Members' (Deficit) Equity		
Liabilities:		
Unearned premiums	\$ 456,258	399,000
Due to related parties	180,041	156,046
Unpaid losses and loss adjustment expenses	365,669	51,018
Unearned advanced premiums	15,524	5,313
Postretirement benefits payable	35,104	25,359
Pension liability	22,869	22,261
Other liabilities	22,308	20,363
Total liabilities	1,097,773	679,360
Members' (deficit) equity	<u>(134,354)</u>	<u>20,635</u>
Total liabilities and members' (deficit) equity	<u>\$ 963,419</u>	<u>699,995</u>

See accompanying notes to statutory financial statements.

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Statutory Statements of Operations and Members' (Deficit) Equity

Years ended December 31, 2004 and 2003

	2004	2003
Underwriting:		
Premiums earned	\$ 809,479	602,050
Less:		
Losses incurred	536,561	275,294
Loss adjustment expenses incurred	130,711	21,810
Underwriting and other expenses incurred	295,351	246,278
	962,623	543,382
Net underwriting (loss) gain	(153,144)	58,668
Investment income	376	265
Other (expense) income:		
Premiums/assessments receivable charged off	(2,470)	(1,526)
Other	250	(384)
Other expense, net	(2,220)	(1,910)
Net (loss) income	(154,988)	57,023
Members' equity (deficit), beginning of year	20,635	(35,633)
Change in nonadmitted assets	(2,743)	(755)
Change in minimum pension liability adjustment (note 4)	2,742	—
Members' (deficit) equity, end of year	\$ (134,354)	20,635

See accompanying notes to statutory financial statements.

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Statutory Statements of Cash Flows

Years ended December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Cash flows from operations:		
Premiums collected, net	\$ 866,511	729,337
Loss and adjustment expenses paid (net of salvage and subrogation)	(328,626)	(224,587)
Underwriting expenses paid	(286,581)	(234,763)
Investment income	376	265
Premiums/assessments receivable charged off	(2,470)	(1,526)
Other income	250	(384)
Net cash from operations	<u>249,460</u>	<u>268,342</u>
Cash flows from financing and other miscellaneous sources:		
Other, net	<u>6,269</u>	<u>(4,150)</u>
Net cash from financing and other miscellaneous sources	<u>6,269</u>	<u>(4,150)</u>
Net increase in cash and cash equivalents	255,729	264,192
Cash and cash equivalents:		
Beginning of year	<u>694,711</u>	<u>430,519</u>
End of year	<u><u>\$ 950,440</u></u>	<u><u>694,711</u></u>

See accompanying notes to statutory financial statements.

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

(1) Summary of Significant Accounting Policies

The statutory financial statements of West Virginia Essential Property Insurance Association (the Association) have been prepared on the basis of accounting practices prescribed or permitted by the National Association of Insurance Commissioners (NAIC) and the Insurance Department of the State of West Virginia.

The more significant accounting policies are as follows:

(a) Premiums

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

(b) Commissions

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

(c) Nonadmitted Assets

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

(d) Unpaid Losses and Loss Adjustment Expenses

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

(e) Use of Estimates

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

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

(f) *Variances from Generally Accepted Accounting Principles*

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

- Commissions and other acquisition costs, if recoverable from future operations, would be deferred and charged against operations on the same basis that related premiums are recognized as revenues.
- Certain assets designated as "nonadmitted" would be reflected in the statutory statement of admitted assets, liabilities, and members' equity (deficit).

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

(g) *Cash and Cash Equivalents*

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

(h) *Reclassifications*

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

(2) *General*

The Association was created by an act of the Legislature of the State of West Virginia to make available basic property insurance against fire and other perils for residential and business properties located in the state. All insurers doing any insurance business in West Virginia of the kinds covered by the Association are required to be a member. Each member participates in the profits and losses of the Association in the proportion that the net direct premiums of the member insurer for the second previous year bear to the net direct premiums written by all members for the second preceding calendar year and is subject to future cash assessments, if required. Members' deficit of \$134,354 at December 31, 2004 will ultimately be assessed to the participating members as required.

The Association shares office space and the services of certain employees with the Insurance Placement Facility of Pennsylvania and the Insurance Placement Facility of Delaware and pays a portion of such joint expenses based on estimates of actual usage.

(3) *Federal Income Taxes*

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

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

(4) Employee Benefits

The Association, in conjunction with the Insurance Placement Facility of Pennsylvania and the Insurance Placement Facility of Delaware and other unaffiliated organizations, is a participant in the Benefits Connection Group Plan, which covers all of its employees. The pension plan qualifies under the provisions of Section 501(a) of the *Internal Revenue Code* and is exempt from federal income taxes. The pension plan is funded through the trustee by contributions to group annuity contracts with two insurance companies.

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

The following table sets forth the year-end status of the plan as it relates to the Association:

	2004	2003
Change in projected benefit obligation:		
Benefit obligation at January 1	\$ 141,526	118,011
Service cost	5,025	3,743
Interest cost	10,954	8,422
Actuarial loss	48,236	14,818
Benefits paid	(5,464)	(3,468)
Benefit obligation at December 31	200,277	141,526
Change in plan assets:		
Fair value of plan assets at January 1	97,435	78,482
Actual return on plan assets	23,562	21,536
Employer contributions	33,028	885
Benefits paid	(5,464)	(3,468)
Fair value of plan assets at December 31	148,561	97,435
Funded status	(51,716)	(44,091)
Unrecognized net actuarial loss	36,862	32,587
	\$ (14,854)	(11,504)

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

	2004	2003
Discount rate	5.75%	6.25%
Rate of compensation increase	3.25	3.50

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

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

	2004	2003
Components of net periodic pension cost:		
Service cost	\$ 5,025	3,743
Interest cost	10,955	8,422
Expected return on plan assets	(10,598)	(6,710)
Amount of loss recognized	2,299	6,049
Net periodic pension cost	\$ 7,681	11,504

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

	2004	2003
Discount rate	6.25%	6.75%
Expected long-term rate of return	8.50	8.50
Weighted average rate of compensation increase	3.50	4.00

The accumulated benefit obligation for the plan was \$171,430 and \$119,696 at December 31, 2004 and 2003, respectively.

Accrued benefit cost recognized in the accompanying statutory statements of admitted assets, liabilities, and members' deficit was \$22,869 and \$22,261 at December 31, 2004 and 2003, respectively.

An additional minimum pension liability (AML) is required when the actuarial present value of the accumulated plan benefit obligation exceeds plan assets and accrued pension liabilities. As of December 31, 2004 and 2003, the Association had an AML of \$8,015 and \$10,757, respectively.

The Association changed the manner in which it accounts for the AML in 2004 to conform to the requirements of SSAP No. 89, *Accounting for Pensions, A Replacement of SSAP No. 8*. Pursuant to the requirements of SSAP No. 89, changes to the AML were recorded directly to members' (deficit) equity. Previously, changes to the AML were recorded through the statutory statement of operations. The decrease in the AML during 2004 was \$2,742 and was credited directly to members' deficit. The decrease in the AML during 2003 was \$6,515 was recorded as a reduction of underwriting and other expenses in the accompanying statutory statement of operations. The accounting change did not have any effect on members' (deficit) equity at December 31, 2004 or 2003.

The benefit obligation excludes liabilities for nonvested employees, which were \$17 and \$199 at December 31, 2004 and 2003, respectively.

The expected long-term rate of return on assets assumption is 8.50%. As defined in *Financial Accounting Standards* (FAS 87), this assumption represents the rate of return on plan assets reflecting the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the benefit obligation. The assumption has been determined by reflecting expectations regarding future rates of

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

return for the investment portfolio, with consideration given to the distribution of investments by asset class and historical rates of return for each individual asset class.

The plan's weighted average asset allocations at December 31, 2004 and 2003, by asset category are as follows:

	2004	2003
Asset category:		
Equity securities	59.0%	61.5%
Debt securities	38.0	38.5
Cash	3.0	—

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

The Association expects to contribute \$8,960 to the plan in 2005.

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

2005	\$	5,960
2006		6,687
2007		7,042
2008		7,912
2009		8,620
2010-2014		60,513

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

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

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

**WEST VIRGINIA ESSENTIAL PROPERTY
INSURANCE ASSOCIATION**

Notes to Statutory Financial Statements

December 31, 2004 and 2003

The following table sets forth the postretirement health care and life insurance benefit plan's funded status as of December 31, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
Accumulated postretirement benefit obligation:		
Postretirement benefit obligation for retirees and fully vested plan participants	\$ 50,188	27,764
Plan assets at fair value	—	—
Accumulated postretirement benefit obligation in excess of plan assets	50,188	27,764
Unrecognized loss	(19,504)	(6,472)
Unrecognized prior service	4,420	4,067
Accrued postretirement benefit cost	<u>\$ 35,104</u>	<u>25,359</u>

The following table represents a reconciliation of postretirement benefit cost for the years ended December 31, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
Accrued postretirement benefit cost at January 1	\$ 25,359	20,211
Benefit expense for year	11,724	6,272
Benefits paid	(1,979)	(1,124)
Accrued postretirement benefit cost at December 31	<u>\$ 35,104</u>	<u>25,359</u>

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

	<u>2004</u>	<u>2003</u>
Discount rate	5.75%	6.25%
Rate of compensation increase	3.50	3.50

Net periodic postretirement benefit cost for 2004 and 2003 includes the following components:

	<u>2004</u>	<u>2003</u>
Service cost	\$ 2,279	5,295
Interest cost	9,389	186
Amortization of loss	774	1,359
Amortization of prior service cost	(718)	(568)
Net periodic postretirement benefit cost	<u>\$ 11,724</u>	<u>6,272</u>

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

	2004	2003
Discount rate	6.25%	6.75%
Weighted average rate of compensation increase	3.50	3.50

For measurement purposes, for participants younger than age 65, healthcare cost trend increases of 12% and 11% were assumed for 2004 and 2003, respectively. These rate increases were assumed to decrease through 2011 and later when they level off at 5%. The healthcare cost trend rate assumption has an effect on the amounts reported. For example, increasing the assumed healthcare cost trend rate by one percentage point in each year would increase the accumulated postretirement benefit obligation as of December 31, 2004 by \$6,478 and net periodic postretirement benefit cost for the year ended December 31, 2004 by \$743.

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

2005	\$	2,218
2006		2,421
2007		2,628
2008		2,972
2009		3,244
2010-2014		21,506

The employees of the Association are eligible to participate in the Benefits Connection Group 401(k) Savings Plan, a defined contribution plan. The plan is administered by the Administration Committee for Benefits Connection Group Savings Plan. Participation in the plan is voluntary. Employees are vested in employer contributions upon participation. Employees may contribute 1% to 16% of their annual compensation on a before-tax basis and/or 1% to 16% of their annual compensation on an after-tax basis for a total of 16%. The Association matches employee contributions up to a maximum of 6% of an employee's annual compensation. Contributions by the Association amounted to \$2,780 and \$2,311 in 2004 and 2003, respectively.

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(5) Liability for Unpaid Losses and Loss Adjustment Expenses

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

	2004	2003
Balance, January 1	\$ 51,018	103,534
Incurred related to:		
Current year	668,845	317,267
Prior years	(1,573)	(20,163)
Total incurred	667,272	297,104
Paid related to:		
Current year	303,176	266,249
Prior years	49,445	83,371
Total paid	352,621	349,620
Balance, December 31	\$ 365,669	51,018

As a result of changes in estimates for anticipated losses and loss adjustment expenses related to insured events of prior years, the liability for losses and loss adjustment expenses decreased by \$1,573 and \$20,163 in 2004 and 2003, respectively.

(6) Lease Commitments

The Association conducts its operations in a leased premises under a lease that will expire April 30, 2008. At December 31, 2004, minimum rental commitments under this noncancelable lease are as follows:

Year ending December 31:		
2005	\$	6,672
2006		6,977
2007		6,977
2008		2,326
Total payments	\$	22,952

Total rental expense was \$7,677 and \$5,986 in 2004 and 2003, respectively.

The Association is charged a portion of the total rentals paid by Insurance Placement Facility of Pennsylvania for common facilities, based upon underwriting activity of the Association during the year. Rental commitment allocations are based upon continuation of the current level of activity.

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(7) Related Party Transactions

The Insurance Placement Facility of Pennsylvania issues all checks, including those payable by the Association, and is then reimbursed by the Association (note 2). Throughout 2004 and 2003, \$352,621 and \$349,620, respectively, was paid by the Insurance Placement Facility of Pennsylvania on behalf of the Association. The related payable to the Insurance Placement Facility of Pennsylvania is \$180,041 and \$156,046 at December 31, 2004 and 2003, respectively.

(8) Annual Statement Reconciliation

The following is a reconciliation between the accompanying statutory financial statements and the annual statement for the years ended December 31, 2004 and 2003:

	2004	
	Net loss	Members' deficit
As reported in the annual statement	\$ (159,103)	(143,755)
2003 underwriting and other expense adjustment	(2,544)	—
2004 underwriting and other expense adjustment	6,659	9,401
As reported herein	\$ (154,988)	(134,354)
	2003	
	Net income	Members' deficit
As reported in the annual statement	\$ 36,724	18,091
2002 underwriting and other expense adjustment	17,755	—
2003 underwriting and other expense adjustment	2,544	2,544
As reported herein	\$ 57,023	20,635

The underwriting and other expense adjustments relate to the additional minimum pension liability adjustments discussed in note 4.