Citizens Property Insurance Corporation

Financial Statements

December 31, 2011 and 2010

Citizens Property Insurance Corporation
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Independent Auditors' Report

The Board of Governors and Management
Citizens Property Insurance Corporation

We have audited the accompanying basic financial statements of Citizens Property Insurance Corporation (Citizens), a component unit of the State of Florida, as of and for the years ended December 31, 2011 and 2010, as listed in the table of contents. These financial statements are the responsibility of Citizens' 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 and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Citizens Property Insurance Corporation as of December 31, 2011 and 2010, and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 21, 2012 on our consideration of Citizens Property Insurance Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 11, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental combining statements of net assets, combining statement of revenues, expenses and changes in net assets, and schedule of supplemental revenues, expenses and claim development information are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Johnson Lambert & Co. LLP

Jacksonville, Florida
May 21, 2011

This discussion provides an assessment by management of the current financial position and results of operations for Citizens Property Insurance Corporation (Citizens or the Company). Management encourages readers to consider the information presented here in conjunction with additional information included in the accompanying financial statements and notes to the financial statements.

Financial Highlights

- The assets of Citizens exceeded its liabilities at the close of the most recent year by $6.0 billion, increasing the net asset position.

- The Company's total net assets increased by $535.1 million. This increase is primarily attributable to net income generated as explained below.

- Operating revenues increased 14% from 2010 to 2011. This increase is the result of the implementation of the glide path rate increase during 2011 as well as an increase in policies in force.

- Operating expenses increased 58% during 2011 as compared to 2010. This increase is primarily due to an increase in losses and loss adjustment expense incurred for the current accident year.

- Nonoperating revenue increased from 2010 to 2011 by 665%, or approximately $80.2 million, due largely to an increase in net investment income.

Overview of Financial Statements

This discussion and analysis is intended to serve as an introduction to Citizens' basic financial statements, which consist of the statements of net assets, statements of revenues, expenses and changes in net assets and the statements of cash flows. This report also contains other supplementary information in addition to the basic financial statements.

The *statements of net assets* present information on all of the Company's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of Citizens is improving or deteriorating.

The *statements of revenues, expenses and changes in net assets* present information showing how the Company's net assets changed during the most recent year. All changes in net assets are reported as soon as the underlying events giving rise to the changes occur, regardless of the timing of related cash flows.

Overview of Financial Statements (Continued)

The *statements of cash flows* present information about the cash receipts and cash payments during the year. The statements show the cash effects of operating, investing and financing transactions during a given period.

The *notes to the financial statements* provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found beginning on page 16 of this report.

In addition to the basic financial statements and accompanying notes, this report also presents certain *supplementary information* concerning the Company's revenues, expenses and claims development information for the last ten policy years.

A summary of Citizens' Statements of Net Assets is presented below *(in thousands)*:

	2011	2010	% Change
Assets			
Current assets	$ 4,128,109	$ 6,216,756	-34%
Capital assets, net	8,834	10,809	-18%
Other noncurrent assets	9,787,045	6,399,103	53%
Total assets	$ 13,923,988	$ 12,626,668	10%
Liabilities			
Current liabilities	$ 3,455,656	$ 3,224,403	7%
Noncurrent liabilities	4,433,540	3,902,595	14%
Total liabilities	7,889,196	7,126,998	11%
Net assets			
Invested in capital assets	8,834	10,809	-18%
Restricted	11,726	13,651	-14%
Unrestricted	6,014,232	5,475,210	10%
Total net assets	6,034,792	5,499,670	10%
Total liabilities and net assets	$ 13,923,988	$ 12,626,668	10%

Assets

As shown above, total assets increased $1.3 billion, or 10%, during 2011 primarily due to the increase in cash and invested assets resulting from the $900 million pre-event bond issuance in July 2011, a considerable increase in premiums collected and a decrease in non-admitted invested assets, partially offset by the $101 million debt maturity of the 2007A HRA Refunding

Financial Analysis (Continued)

Assets (Continued)

Bonds in March 2011, the $500 million debt maturity of the 2010A-2 HRA Bonds in April 2011, and the $250 million debt maturity of the 2008A-1 HRA Bonds in June 2011. Certain investments, representing less than 2% of the portfolio continue to be in defaulted Structured Investment Vehicles (SIVs) for which the Company continues to receive payments of principal and interest. Declines in market value of invested assets are continually evaluated to determine whether these declines are temporary or other-than-temporary in nature. In making this determination, the Company monitors external impairment indicators such as issuer credit ratings as well as the extent and duration of the related declines and internal impairment indicators such as the Company's intent and ability with respect to retention of the impaired securities. These indicators are obtained from both third-party valuation services and internal analyses performed by the Company. No such other-than-temporary declines in market value have been recorded in 2011 or 2010. However, it is noteworthy to mention that $100.5 million of other-than-temporary impairment recorded in 2007 and 2008 has been recovered as of December 2011. During 2010, total assets increased $3.3 billion, or 36%, primarily due to the increase in cash and invested assets resulting from the $2.4 billion pre-event bond issuance and a considerable increase in premiums collected offset by the $96.2 million debt service payment on the 2007A HRA Refunding Bonds in March 2010 and the $625.0 million debt maturity on the 2009A-2 HRA Bonds in June 2010.

Current assets include cash, cash equivalents, and short-term investments of $3.6 billion and $5.7 billion for the years ended 2011 and 2010. Long-term investments totaled $9.3 billion and $5.7 billion for the years ended 2011 and 2010. The increase in invested assets is the result of the $900 million bond issuance, net cash flows from 2011 operations, the collection of emergency assessment funds, and Florida Hurricane Catastrophe Fund (FHCF) reimbursements received during 2011 partially offset by the $851 million of total debt maturities during the first half of 2011. During 2010, invested assets increased 3.1 billion, or 36%, due to the $2.4 billion bond issuance, net cash flow from 2010 operations, the collection of emergency assessment funds, and Florida Hurricane Catastrophe Fund (FHCF) reimbursements received during 2010 offset by the maturity of the $625.0 million bonds and the $96.2 million debt service payment made in 2010.

During the year, Citizens had no significant capital asset activity.

Liabilities

Total liabilities increased $762.2 million, or 11%, during 2011. This increase is due primarily to an increase in loss reserves, loss adjustment expense reserves and unearned premiums. During 2010, total liabilities increased $2.3 billion, or 47% due primarily to an increase in unearned premiums, unearned assessment income and long-term debt.

Financial Analysis (Continued)

Liabilities (Continued)

Current liabilities are comprised primarily of loss reserves, loss adjustment expense (LAE) reserves, unearned premium, the current portion of unearned assessment income and the current portion of long-term debt. Loss and LAE reserves increased $490.3 million, or 57%, from 2010 to 2011. Net loss and LAE reserves related to the 2004 and 2005 hurricanes were $128.3 million as of December 31, 2011 as compared to $102 million as of December 31, 2010. The increase in 2011 is largely due to the Hurricane Wilma commutation with the FHCF.

Unpaid loss and LAE reserves not related to hurricanes increased from $754 million as of December 31, 2010 to $1.22 billion as of December 31, 2011. The increase in both 2011 and 2010 is due largely to increases in overall exposure and of sinkhole, fire, theft and water claims.

Unearned premiums increased $230.7 million, or 19% from 2010 to 2011, which is primarily due to an increase in premium written. During 2010 unearned premiums increased $211.1 million, or 21%, primarily due to an increase in premium written.

Unearned assessment income decreased $56.9, or 27% at December 31, 2011 compared to December 31, 2010. This decrease is consistent with the earnings elapsed since 2010. During 2010, unearned assessment income increased $213.5 million, or 100%. This increase is due to a prior period correction to record the unearned portion of the financing cost for the post event bonds related to the 2005 HRA emergency assessment.

Reinsurance premiums payable increased $55.7 million, or 100%. This increase is the result of the remaining premium installment of $55.7 million due for the 2011 private reinsurance program. Private reinsurance was not purchased during 2010 and therefore no reinsurance premiums were payable as of December 31, 2010.

Operating Revenue

A summary of Citizens Statements of Revenues, Expenses and Changes in Net Assets and certain key financial ratios are presented below *(in thousands)*:

	2011	2010	% Change
Operating revenue			
Premiums earned	$ 2,251,731	$ 1,971,649	14%
Operating expenses			
Losses and LAE incurred	1,354,836	762,934	78%
Other underwriting expenses	429,791	363,243	18%
Total expenses	1,784,627	1,126,177	58%
Operating income	467,104	845,472	-45%
Nonoperating revenues	68,136	(12,053)	-665%
Change in net assets	$ 535,240	$ 833,419	-36%
Policies in force	1,472,391	1,283,538	15%
Underwriting ratios			
Loss and LAE ratio (calendar year)	60%	39%	21%
Expense ratio	14%	14%	0%
Combined ratio	74%	53%	21%

Direct written premium increased 18% to $3.1 billion as of December 31, 2011 compared to $2.6 billion as of December 31, 2010. This increase is the result of the implementation of the glide path rate increase during 2011 as well as a 15% increase in policies in-force. Net earned premiums increased to $2.3 billion at December 31, 2011 as compared to $2.0 billion at December 31, 2010, an increase of 280.1 million, or 14%. Direct premium written increased 19% to $2.6 billion as of December 31, 2010 compared to $2.2 billion as of December 31, 2009 due primarily to the implementation of the glide path rate increase during 2010 as well as an increase in the policies in force. Net earned premiums increased to $2.0 billion at December 31, 2010 as compared to $1.7 billion at December 31, 2009, an increase of 260.2 million, or 15%. The 2010 in force policy count increased 25% as compared to 2009.

Financial Analysis (Continued)

Operating Revenue (continued)

Historically, Citizens' rates were required to be actuarially sound and not competitive with approved rates charged by authorized insurers. However, during a 2007 special legislative session, the standards that Citizens uses to set rates were changed by removing the requirement that Citizens develop rates that are not competitive with approved rates charged by authorized insurers. The requirement that rates be actuarially sound remains.

Also, the 2007 Special Legislation rescinded the rates for Citizens premiums which took effect January 1, 2007, except for rates which were lowered. Such legislation required Citizens, as of January 1, 2007, to use the lower rates that were in effect on December 31, 2006 and to provide refunds to policyholders who had paid higher rates as a result of that rate filing. This requirement produced a reduction to the homeowner multiperil rates and residential fire/dwelling rates of 11.0% and 17.4% respectively, and decreased residential wind-only rates for the Costal Account 18.2%. Also per the Special Legation, the rates in effect on December 31, 2006 remained in effect through December 31, 2009.

During the 2009 legislative session, Citizens' statute was amended to require that beginning on July 15, 2009 and each year thereafter, the Corporation must make a recommended actuarially sound rate filing for each personal and commercial line of business it writes, to be effective no earlier than January 1, 2010. In addition, the new law requires that Citizens implement such rate increases so that the rate increase per policyholder does not exceed 10 percent, excluding coverage changes and surcharges.

Premiums ceded to the FHCF totaled $453.1 million and $368.1 million during 2011 and 2010, respectively, and are included in net earned premiums. The increase in FHCF premium is attributed primarily to an increase in overall FHCF eligible exposure. The Corporation did not enter into excess of loss reinsurance agreements with private reinsurers in 2011 or 2010.

Ceded premiums to takeout companies as of December 31, 2011 increased $22.7 million, or 104%, compared to the same period in 2010. Although the number of policies assumed, as well as related premium, decreased from 2010 as compared to 2011, there were a significant number of opt-outs that occurred in 2010 which served to decrease the ceded premium. Ceded premiums to takeout companies decreased $79.0 million, or 78%, during 2010. During 2010, $21.7 million was ceded to takeout companies compared to $100.8 million ceded during 2009.

Operating Expenses

Losses and LAE incurred increased $591.9 million, or 78%, in 2011 as compared to 2010. This increase is largely attributable to an increase in the amount of sinkhole claims being reported in 2011 for both prior accident periods as well as the current accident period; a 71% increase to

Financial Analysis (Continued)

Operating Expenses (Continued)

4,226 claims in 2011 from 2,465 claims in 2010. Losses and LAE incurred increased $181.8 million, or 31%, in 2010 as compared to 2009, due mainly to the non-catastrophic claims costs that relate to water, sinkhole and fire claims. The frequency and severity of such claims has increased over time. This is coupled by a minor amount of adverse development during 2010 related to prior year storms, as well as an increase in policy and claim counts.

Other underwriting expenses increased $66.5 million, or 18%, in 2011. Certain underwriting expenses such as agent commissions and premium taxes, are determined based on written premiums and will increase proportionately. During 2011, commission and premium and other tax expenses consisted of 54% and 11% of other underwriting expenses, respectively. During 2010, commission and premium and other tax expenses consisted of 53% and 10% of other underwriting expenses, respectively.

Non-operating Income (Expenses)

Non-operating income/expenses consist mainly of assessment income, net investment income, and interest expense. Non-operating income increased $80.2 million, or 665% in 2011 as compared to 2010 which corresponds with the increase in net investment income of $84.4 million, or 72%. The increase in net investment income is mainly attributed to the increase in the weighted average of maturity duration in the new investment policy, an increase in allocations to external investment managers and an increase in total asset portfolio. In addition, line of credit fees and note issuance costs decreased $3.9 million, or 57%, offset by a decrease in assessment income of $7.6 million, or 12%. Non-operating expense decreased $21.5 million, or 64% in 2010 as compared to 2009 which corresponds with the increase in assessment income of $64.6 million, or 100%. The increase in assessment income is due to the earning of the portion of the unearned post event financing costs related to the 2005 HRA emergency assessment. In addition, net investment income increased $5.8 million, or 5%, offset by an increase in interest expense of $56.2 million, or 43% due primarily to the issuance of the $2.4 billion bonds during 2010.

Economic Factors

Citizens' management performs an evaluation of pre-event liquidity needs in advance of each hurricane season. As a governmental entity, Citizens has the ability to issue municipal debt on a taxable or tax-exempt basis. Pre-event bond proceeds may be accessed as needed and as permitted by the bond documents. Bank credit lines may also be a component of the pre-event liquidity program. Subsequent to year end 2007, management determined that its 2004, 2006, and 2007 auction rate securities were no longer an appropriate venue to provide liquidity given the increased interest rates required to be paid as a result of the industry-wide market turmoil of

Financial Analysis (Continued)

Economic Factors (continued)

late 2007 and early 2008. These securities were redeemed in 2008. As described in Notes 7 and 10 Citizens issued fixed rate tax-exempt debt in 2011, 2010, 2009, and 2008 to fulfill its liquidity needs. Bank credit lines were secured in 2009 and 2008 to provide pre-event liquidity for those hurricane seasons.

Citizens' Coastal Account bond ratings are A2 / A+ / A+ from Moody's / Standard & Poor's / Fitch. The Coastal Account's Short-Term ratings are MIG1 / SP-1+ / F1+ from Moody's / Standard & Poor's / Fitch. In July 2011, Standard & Poor's changed Coastal Account's ratings outlook from negative to Stable. Moody's and Fitch also have Stable outlook on its ratings. The ratings reflect only the views of such organizations and any desired explanation of the significance of such ratings should be obtained from the rating agency furnishing the same, at the following addresses: Moody's, 7 World Trade Center at 250 Greenwich Street, New York, New York 10007, Standard &Poor's , 55 Water Street, New York, New York, 10041, and Fitch, Inc. One State Street Plaza, New York, NY 10004. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant.

During 2011, management continued to administer programs designed to reduce the number of polices written by Citizens. Citizens' statutory mission includes providing property insurance to applicants who are in good faith entitled to obtain affordable insurance through the voluntary market but are unable to do so. Citizens' depopulation program is designed to return policies to the voluntary market.. The private market has responded by removing policies from the Personal Lines Account, the Commercial Lines Account and the Coastal Account; depopulation tends to be most significant for the Personal Lines Account. During 2011, 45,827 PLA policies and 7,750 Coastal policies were assumed by private insurers, as compared to 57,561 PLA policies and 2,231 Coastal policies assumed during 2010 and 132,803 PLA policies and 16,842 Coastal policies assumed during 2009 and 362,964 PLA policies, 601 CLA policies and 21,519 Coastal policies assumed during 2008 and 247,923 PLA policies assumed during 2007 and 26,225 PLA policies and 41,628 Coastal policies assumed during 2006. Takeout activity decreased in 2011 as compared to 2010 largely due to Florida property insurance market conditions.

Citizens' enabling legislation and Plan of operations established a process by which Citizens Board of Governors levies assessments to recover any deficits incurred in a given year. Citizens' determination of the amount of assessment is subject to the verification of the mathematical calculation by the Office of Insurance Regulation. Citizens' ability to assess provides some assurance of its financial stability.

Citizens Property Insurance Corporation
Statements of Net Assets

	December 31 2011	December 31 2010
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	$ 1,575,852	$ 1,877,644
Short-term investments	1,999,099	3,837,405
Restricted cash and cash equivalents	11,726	13,651
Deferred policy acquisition costs	144,947	130,647
Investment income due and accrued	72,831	43,539
Prepaid reinsurance premiums	25,889	16,617
Reinsurance recoverable on paid losses and LAE	3,130	11,610
Premiums receivable	181,018	153,584
Premiums receivable from assuming companies	874	3,081
Current portion of deferred financing costs	22,795	22,840
Current portion of assessment receivable	89,948	106,138
Total current assets	4,128,109	6,216,756
Noncurrent assets:		
Long-term investments	9,303,068	5,726,480
Capital assets	8,834	10,809
Deferred financing costs	83,785	101,368
Assessment receivable	391,354	567,640
Other assets	8,838	3,615
Total noncurrent assets	9,795,879	6,409,912
Total assets	$ 13,923,988	$ 12,626,668

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Net Assets (Continued)

	December 31 2011	December 31 2010
	(In Thousands)	
Liabilities and net assets		
Current liabilities:		
Loss reserves	$ 1,093,917	$ 680,701
Loss adjustment expense reserves	252,653	175,564
Unearned premiums	1,437,120	1,206,443
Current portion of unearned assessment income	48,881	56,941
Reinsurance premiums payable	55,684	-
Advance premiums and suspended cash	99,291	105,936
Interest payable	27,479	34,938
Taxes and fees payable	6,477	4,317
Current portion of long-term debt	317,485	850,995
Other current liabilities	116,669	108,568
Total current liabilities	3,455,656	3,224,403
Noncurrent liabilities:		
Unearned assessment income	107,709	156,590
Long-term debt	4,325,831	3,746,005
Total noncurrent liabilities	4,433,540	3,902,595
Total liabilities	7,889,196	7,126,998
Net assets:		
Invested in capital assets	8,834	10,809
Restricted	11,726	13,651
Unrestricted	6,014,232	5,475,210
Total net assets	6,034,792	5,499,670
Total liabilities and net assets	$ 13,923,988	$ 12,626,668

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Revenues, Expenses and Changes in Net Assets

	Years Ended December 31 2011	2010
	(In Thousands)	
Operating revenue:		
Premiums earned	$ 2,251,731	$ 1,971,649
Operating expenses:		
Losses incurred	1,107,600	603,911
Loss adjustment expenses incurred	247,236	159,023
Service company fees	9,317	8,305
Agent commissions	230,926	193,482
Taxes and fees	45,419	35,778
Processing and other fees	1,403	1,465
Other underwriting expenses	146,980	122,620
Takeout bonus expense (income)	(4,254)	1,593
	1,784,627	1,126,177
Operating income	467,104	845,472
Nonoperating revenues (expenses):		
Net investment income	201,013	116,644
Interest expense	(189,643)	(188,066)
Assessment income	56,941	64,570
Line of credit fees and note issuance costs	(6,915)	(10,828)
Other income	6,740	5,627
Total nonoperating revenues (expenses)	68,136	(12,053)
Change in net assets	535,240	833,419
Net assets, beginning of year	5,499,670	4,447,538
Other changes in net assets	(118)	218,713
Net assets, end of year	$ 6,034,792	$ 5,499,670

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Cash Flows

	Years Ended December 31 2011	2010
	(In Thousands)	
Cash flows from operating activities		
Premiums collected, net of reinsurance	$ 2,449,744	$ 2,214,911
Losses and loss adjustment expenses paid	(864,531)	(648,816)
Payments to employees for services	(68,605)	(66,436)
Payments for underwriting expenses	(294,760)	(323,094)
Net cash provided by operating activities	1,221,848	1,176,565
Cash flows from noncapital financing activities		
Debt issuance	900,000	2,467,374
Debt redemption	(850,995)	(721,760)
Interest paid	(199,791)	(199,917)
Assessment income received	192,476	246,293
Financing costs paid	10,713	(702)
Net cash provided by noncapital financing activities	52,403	1,791,288
Cash flows from capital and related financing activities		
Capital assets acquired	(2,667)	(1,689)
Net cash used in capital and related financing activities	(2,667)	(1,689)
Cash flows from investing activities		
Proceeds from investments sold, matured or repaid	9,314,626	21,834,152
Investments acquired	(10,889,927)	(26,141,949)
Change in restricted cash	1,925	758
Net cash used in investing activities	(1,573,376)	(4,307,039)
Net decrease in cash and cash equivalents	(301,792)	(1,340,875)
Cash and cash equivalents:		
Beginning of year	1,877,644	3,218,519
End of year	$ 1,575,852	$ 1,877,644

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Cash Flows (Continued)

	Years Ended December 31 2011	2010
	(In Thousands)	
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 467,104	$ 845,472
Adjustments to reconcile net cash provided by operating activities:		
Depreciation expense	4,642	9,551
(Increase) decrease in operating assets:		
Deferred policy acquisition costs	(14,300)	(33,269)
Prepaid reinsurance premiums	(9,272)	31,668
Reinsurance recoverable	8,480	11,901
Premiums receivable, net	(25,227)	(31,822)
Deferred takeout bonus	-	1,722
Other assets	1,517	4,947
Increase (decrease) in operating liabilities:		
Loss and loss adjustment expense reserves	490,305	114,118
Unearned premiums	230,677	211,115
Reinsurance premiums payable	55,684	(35,076)
Advance premiums and suspended cash	(6,645)	20,400
Taxes and fees payable	2,160	1,495
Other current liabilities	16,841	24,433
Other changes in net assets	(118)	(90)
Net cash provided by operating activities	$ 1,221,848	$ 1,176,565

See accompanying notes to financial statements.

NOTE 1 - GENERAL

Citizens Property Insurance Corporation (Citizens or the Corporation) was established on August 1, 2002, pursuant to Section 627.351(6), Florida Statutes (the Act), to provide certain residential and non-residential property insurance coverage to qualified risks in the State of Florida under circumstances specified in the Act. The original intent of the legislation was that property insurance be provided through Citizens to applicants who are in good faith entitled to procure insurance through the voluntary market but are unable to do so. Citizens results from a combination of the Florida Residential Property and Casualty Joint Underwriting Association (the FRPCJUA) and the Florida Windstorm Underwriting Association (the FWUA). The FRPCJUA was renamed Citizens and the FWUA's rights, obligations, assets, liabilities and all insurance policies were transferred to Citizens. Unlike private insurers offering coverage through the admitted market, Citizens is not required to obtain or to hold a certificate of authority issued by the Florida Office of Insurance Regulation (the Office). For purposes of its tax-exempt status, Citizens is considered a political subdivision and an integral part of the State of Florida. As such, Citizens' operations may be affected by the legislative process. In 2007, the Act was amended to recognize Citizens' status as a governmental entity and to add affordability as an element of Citizens' statutory mission.

Citizens operates pursuant to a Plan of Operation (the Plan) approved by the Financial Services Commission (the Commission) of the State of Florida. The Commission is composed of the Governor, the Chief Financial Officer, the Attorney General and the Commissioner of Agriculture of the State. Prior to October 1, 2006, the Plan was subject to the approval of the Office.

Citizens is supervised by a Board of Governors (the Board) which consists of eight individuals who reside in the State of Florida. The Governor, the Chief Financial Officer, the President of the Senate and the Speaker of the House of Representatives each appoint two members of the Board. At least one of the two members appointed by each appointing officer must have a demonstrated expertise in the insurance industry. The Chief Financial Officer designates one of the appointees as the Board's chair. All Board members serve at the pleasure of their appointing officers.

Citizens' president (executive director) and senior managers are engaged by and serve at the pleasure of the Board. The president is subject to confirmation by the Florida Senate.

Criteria for defining the reporting entity are identified and described in the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards, Sections 2100 and 2600. Application of these criteria determines potential component units for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the primary government's financial statements to be misleading or incomplete. Based on the application of these criteria, Citizens is a component unit of the State of Florida, and its financial activity is reported in the state's Comprehensive Annual Financial Report by discrete presentation.

NOTE 1 - GENERAL (CONTINUED)

The financial statements presented herein relate solely to the financial position and results of operations of Citizens and are not intended to present the financial position of the State of Florida or the results of its operations or its cash flows.

Citizens has determined that it has no component units that should be included in its separately reported financial statements. However, the Florida Market Assistance Plan (FMAP) is a financially related entity. FMAP is a 501(c)(6) entity created by Section 627.3515, Florida Statutes. FMAP was created for the purpose of assisting in the placement of applicants who are unable to procure property or casualty insurance coverage from authorized insurers when such insurance is otherwise generally available. As provided in FMAP's enabling legislation, each person serving on the Board of Citizens also serves on the Board of FMAP. In addition, Citizens is required to fund any deficit incurred by FMAP in performing its statutory purpose. Citizens is not required to include FMAP as component unit in its financial statements because FMAP's total assets and total revenue are not significant to Citizens.

Pursuant to the Act, all revenues, expenses, assets and liabilities of Citizens shall remain divided into three separate accounts: the Personal Lines Account, the Commercial Lines Account and the Coastal (formerly the High-Risk) Account. A brief history of each account follows:

Personal Lines Account History - The Florida Residential Property and Casualty Joint Underwriting Association began operations on January 21, 1993, after Hurricane Andrew, pursuant to Section 627.351(6), Florida Statutes, to provide certain residential property insurance coverage to qualified risks in the State of Florida to applicants who were in good faith entitled to procure insurance through the private market but were unable to do so. Residential property coverage consists of the types of coverage provided to homeowners, mobile homeowners, tenants, condominium unit owners, and similar policies. The policies provide coverage for all perils covered under a standard residential policy, subject to certain underwriting requirements. Such policies may exclude windstorm coverage on property within eligible areas. This portion of the FRPCJUA's activities became the Personal Lines Account under Citizens.

Commercial Lines Account History **–** The Florida Property and Casualty Joint Underwriting Association (FPCJUA) was activated in early 1994 to provide commercial residential coverage, i.e., coverage for condominium associations, apartment buildings and homeowner associations, to organizations unable to obtain such coverage from a private insurer. During 1995, legislation was enacted to transfer all obligations, rights, assets, and liabilities related to commercial residential coverage from the FPCJUA to the FRPCJUA. The legislation required that the premiums, losses, assets and liabilities be accounted for separately from the FRPCJUA's personal residential business. This portion of the FRPCJUA's activities became the Commercial Lines Account under Citizens. In 2006, the FPCJUA was re-activated to provide commercial non-residential wind-only coverage. In 2007, legislation was enacted which resulted in the transfer and assumption of the FPCJUA's commercial non-residential policies by Citizens. These policies were added to the Commercial Lines Account.

NOTE 1 - GENERAL (CONTINUED)

Coastal Account History – The Florida Windstorm Underwriting Association, which was a residual market mechanism for windstorm and hail coverage in select areas of the State, was created by an act of the Florida Legislature in 1970 pursuant to Section 627.351(2), Florida Statutes. FWUA was a Florida unincorporated association, the members of which were all property insurance companies holding a certificate of authority to provide property insurance coverage in the State. FWUA provided policies of windstorm insurance for property owners within the eligible areas who were unable to obtain such coverage from private insurers. Insured properties include personal residential, commercial residential and commercial non-residential properties. This portion of the FWUA's activities became the High Risk Account under Citizens. In 2007, Citizens received authority to issue multi-peril policies in the High-Risk Account. Pursuant to legislative changes during 2011, the High-Risk Account was renamed the Coastal Account.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accounting policies and practices of Citizens conform to accounting principles generally accepted in the United States applicable to a proprietary fund of a government unit. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. Citizens applies all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) statements, interpretations and codification, Accounting Principles Board (APB) Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Citizens' has also elected to apply all FASB statements and interpretations issued after November 30, 1989 except for those that conflict with or contradict GASB pronouncements.

GASB Statement No. 34 established standards for financial reporting for all state and local governmental entities, which includes a Statement of Net Assets, a Statement of Revenues, Expenses, and Changes in Net Assets, and a Statement of Cash Flows. It requires net assets to be classified and reported in three components: invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (Continued)

net assets component as the unspent proceeds. As of December 31, 2011 and 2010, Citizens did not have any outstanding debt that was attributable to capital assets.

- Restricted net assets – This component of net assets includes assets subject to external constraints imposed by creditors (such as through debt covenants), grantors, contributors, laws or regulations of other governments, or constraints imposed by law through constitutional provisions or enabling legislation.

- Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Use of Estimates

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

Measurement Focus

The financial statements of proprietary funds are prepared using the economic resources measurement focus and the accrual basis of accounting. All assets and liabilities associated with the operations of Citizens are included in the statements of net assets. The Statements of Revenues, Expenses and Changes in Net Assets presents increases (revenues) and decreases (expenses) in total net assets. The Statements of Cash Flows provides information about how Citizens finances and meets the cash flow needs of its activities.

Correction of an Error

Effective January 1, 2010, Citizens recorded a prior period adjustment relating to previously unrecognized additional financing costs on the 1999 HRA bonds that occurred during the 2007 HRA post event bond issuance. The effect of the entry was as follows *(in thousands)*:

	Pre-correction balance at January 1, 2010	Correction of error adjustment	Post-correction balance at January 1, 2010
Assessments receivable	$ 423,167	$ 496,903	$ 920,070
Net assets	4,447,538	218,803	4,666,341
Unearned assessment income	-	278,101	278,101

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Correction of an Error (Continued)

The effect of the correction of the error is included in the Statements of Revenues, Expenses and Changes in Net Assets.

Cash, Cash Equivalents, and Investments

Cash consists of demand deposits held with financial institutions, various highly liquid money market funds, other short term corporate obligations and agency discount notes. Highly liquid investments with original maturities of three months or less at the time of acquisition are considered to be cash.

Investments consist of fixed-income securities and small portion in the SBA Florida Prime. Such investments are recorded at fair value, which is generally based on independent quoted market prices. If quoted market prices are not available, broker quotes or an estimation of the current liquidation values is determined through a collaborative process among various pricing experts and sources in the marketplace. Changes in fair value are reflected as a component of net investment income. Citizens considers all investments with remaining maturities of one year or less to be short-term and all investments with remaining maturities of less than 3 months to be cash equivalents.

Deferred Policy Acquisition Costs

Costs that are directly related to the successful acquisition of new or renewal policies are deferred and recognized over the term of the related policy. In October 2010, the Financial Accounting Standards Board (FASB) amended Topic 944 to revise the definition of *acquisition costs*. Generally, this revision narrowed the scope and definition of acquisition costs that may be capitalized. This amendment is effective for fiscal years beginning after December 15, 2011, with early adoption permitted. Citizens elected to early adopt for the fiscal year beginning January 1, 2011. Acquisition costs that are capitalized by Citizens consist of servicing carrier fees, producer commissions, ceding commissions, premium taxes, and other underwriting expenses comprised largely of reinspection fees, geographical data services and ISO fees. Amortization of deferred policy acquisition costs recognized for the years ended December 31, 2011 and 2010 was $304.1 million and $254.4 million, respectively. Had Citizens not elected to early adopt the amended topic 944, amortization of deferred policy acquisition costs for the year ended December 31, 2011 would have been $312.1 million.

Deferred Takeout Bonus

Takeout bonuses incurred in connection with the depopulation of Citizens are deferred and amortized over the term of the related agreement under which the policy is removed from Citizens, which is generally a three-year period. Recoveries are recorded as a contra expense once it is determined that the assumed policy is no longer bonus eligible.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Assets

Capital assets are stated at cost less related accumulated depreciation. The capitalization threshold for assets purchased is $2,500. Depreciation is computed using the straight-line method over the estimated useful lives of three to seven years. Depreciation expense for capital assets was $4.6 million and $9.6 million for the years ended December 31, 2011 and 2010.

Loss Reserves and Loss Adjustment Expense Reserves

Liabilities for loss reserves and loss adjustment expense reserves are estimated based on claims adjusters' evaluations and on actuarial evaluations, using Citizens' loss experience and industry statistics. While the ultimate amount of losses and loss adjustment expenses incurred is dependent on future development, in management's opinion, the estimated reserves are adequate to cover the expected future payment of losses. However, the ultimate settlement of losses may vary significantly from the reserves provided. Adjustments, if any, to estimates recorded resulting from subsequent actuarial evaluations or ultimate payments will be reflected in operations in the period in which such adjustments are known or estimable. Citizens does not discount liabilities for loss reserves and loss adjustment expense reserves.

Premiums

Premiums written are recorded on the effective date of the policy and earned using the daily pro rata basis over the policy period. The portion of premiums not earned at the end of the period are recorded as unearned premiums.

Premiums receivable includes amounts due from policyholders for billed premiums. Billings are calculated using estimated annual premiums for each policy and are paid either through an installment plan offered by Citizens or in their entirety at the inception of the policy. An allowance for doubtful accounts is recorded for the estimated uncollectible amounts, and amounted to $2.5 million and $2.5 million at December 31, 2011 and 2010, respectively.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from premiums charged to policyholders. Operating expenses include incurred losses, loss adjustment expenses and necessary costs incurred to provide and administer residential and commercial property insurance coverage and to carryout programs for the reduction of new and renewal writings.

Assessments

Citizens' assessments made pursuant to the Act and the Plan are recognized as revenue and recorded as receivable in the period approved by Citizens' Board and verified by the Office for mathematical accuracy. Assessment receivables are considered to be fully collectible. Unearned

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Assessments (Continued)

assessment income consists of the additional financing costs related to the HRA post-event bond issuance.

Reinsurance

Premiums ceded under reinsurance agreements are recorded as a reduction of earned premiums. Reinsurance recoverables on unpaid losses are recorded as a reduction of losses incurred and loss adjustment expenses incurred. Reinsurance recoverables on paid losses are recorded as receivables. All catastrophe reinsurance payments are recorded as premiums ceded and are amortized over the life of the hurricane season for which the payments apply. Premiums ceded include both FHCF and private catastrophic reinsurance purchases and depopulation premiums.

Note Issuance Costs

Note issuance costs incurred in connection with issuing notes payable are deferred and amortized over the life of the note agreements.

Market Risk

Citizens' underwrites residential and commercial property insurance policies in the State of Florida. Therefore, adverse economic changes or certain changes in the insurance laws of the State of Florida could have a significant impact on Citizens' future financial position and results of operations. Approximately 52% of Citizens' insurance coverage exposure lies in the Southeast Florida counties of Miami-Dade, Broward, Monroe and Palm Beach at December 31, 2011. Approximately 14% of Citizens' insurance coverage lies in Pinellas andHillsborough counties as of December 31, 2011. Severe storm activity in any of these counties, or throughout the State of Florida, could have a significant impact on Citizens' future financial position and results of operations. Unlike private insurers that are subject to liquidation in the event of insolvency, Citizens is able (and statutorily required) to levy surcharges and assessments in the event of a deficit in any or all of its accounts. (See Note 16).

Concentration of Credit Risk

Financial instruments that potentially subject the Corporation to concentrations of credit risk consist principally of cash and cash equivalents, and investments. The Company's cash management and investment policies restrict investments by type, credit and issuer, and the Company performs periodic evaluations of the credit standing of the financial institutions with which it deals. As of December 31, 2011, management believes the Company had no significant concentrations of credit risk other than those disclosed in Note 3.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Subsequent Events

Citizens has evaluated subsequent events for disclosure and recognition through May 21, 2012, the date on which these financial statements were available to be issued.

NOTE 3 - INVESTMENTS

Citizens' invested assets are governed by four investment policies, two for taxable operating funds and two for tax-exempt bond proceeds:

- Liquidity Fund (Taxable): generally this policy will govern the investment of funds and surplus that, in addition to internally managed cash, will be the first moneys used to pay claims after an event, and that can be used to pay operating expenses on an ongoing basis.

- Liquidity Fund (Tax-Exempt): generally this policy will govern the investment of tax-exempt pre-event bond proceeds and other moneys required to be invested in tax-exempt instruments. Citizens will use these monies to pay claims after an event or to pay principal and / or interest payments on as needed basis.

- Claims-Paying Fund (Taxable): generally this policy will govern the investment of funds that will be used to pay post-event claims after Citizens has expended all moneys in the Liquidity Fund. Only moneys eligible for investment in taxable instruments will be deposited in this fund.

- Claims-Paying Fund (Tax-exempt): generally this policy will govern the investment of tax-exempt pre-event bond proceeds and other moneys required to be invested in tax-exempt instruments. Citizens will use these moneys to pay claims after an event, typically after it has spent all funds in the Liquidity Fund.

The Liquidity Fund taxable policy requires a minimum of half of all securities in its portfolio to be U.S. Government or U.S. Government Agency fixed income securities while the remaining half may be corporate fixed income securities rated A2/A/A or better by Moody's, S&P or Fitch, respectively, at the time of purchase. The Claims Paying Fund taxable policy requires a minimum of 40% of all securities in its portfolio to be U.S. Government or U.S. Government Agency fixed income securities while the remaining 60% may be corporate fixed income securities rated A2/A/A or better by Moody's, S&P and/or Fitch at the time of purchase. The Liquidity Fund and Claims Paying Fund tax-exempt policies require all securities be invested in tax exempt fixed income securities not subject to the federal alternative minimum tax rated A2/A equivalent or better by Moody's and S&P at the time of purchase. The investment policies provide that a significant portion of Citizens' assets should be in relatively short duration instruments and the majority of Citizens' assets should have a weighted duration consistent with the objectives of maximizing return without exposure to interest rate risk. Citizens may invest in

NOTE 3 – INVESTMENTS (CONTINUED)

fixed or variable rate instruments that have minimum ratings as specified in the investment policy by one of the Rating Agencies. Investments in the Liquidity Fund portfolios (taxable and tax-exempt) may have a maximum maturity of 39 months and the weighted average maturity cannot exceed 365 days. Investments in the Claims Paying Fund portfolios (taxable and tax-exempt) may have a maximum maturity of 61 months and the weighted average maturity cannot exceed 3 years. In accordance with Citizens' applicable taxable and tax-exempt investment policies the majority of Citizens' bond proceeds and operating cash are managed by independent investment management firms engaged by Citizens and in part by Citizens' staff. Permitted investments generally must be rated in one of the two or three highest rating categories of each of the Rating Agencies (Moody's and S&P), depending on the type of investment.

Citizens' short-term investments include shares held in the Florida State Board of Administration's Florida Prime ("SBA Florida Prime"), formerly known as the Florida State Board of Administration's Local Government Investment Pool. The entire $30.3 million invested in the SBA Florida Prime at December 31, 2011 is invested in Fund B, which has been frozen from investor withdrawals due to that portfolio's investment in distressed illiquid assets. As principal and interest payments are received, Citizens' allocable portion is eligible for withdrawal and such withdrawals have been consistently made. Fund B is accounted for as a fluctuating net asset value pool, which had a market value factor at December 31, 2011 of 0.7657. Fund B is not rated by any nationally recognized statistical rating agency. Citizens withdrew $8.5 million and $20.1 million, during 2011 and 2010, respectively. Full realization of the principal value of Pool B assets is not readily determinable.

Citizens investment policy for bond proceeds is at least or more restrictive than the bond documents require.

- ***Credit Risk Disclosure -*** Credit risk exists when there is a possibility the issuer or other counterparty to an investment may be unable to fulfill its obligations. With the exception of the default securities representing less than 2% of the investment portfolio, all long-term and short-term securities held in the investment portfolio are rated by two of the three nationally recognized rating agencies. The following table presents the fair value by rating classification as reported by Moody's. (See discussion of rating agencies in "Economic Factors" under "Management's Discussion & Analysis").

NOTE 3 – INVESTMENTS (CONTINUED)

Rating	Fair Value *(in thousands)*
A1	$ 838,991
A2	793,373
A3	7,090
AA	-
AA1	1,404,227
AA2	1,693,274
AA3	1,166,866
AAA	4,894,156
BAA	47,105
MIGI	72,303
P-1	171,874
Default	211,887
Loan backed and structured securities	1,021
	$ 11,302,167

- ***Custodial Risk Credit -*** For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, Citizens would not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Citizens had no investments with custodial credit risk as of December 31, 2011 and 2010, respectively. All investments were held by Citizens or its agent in Citizens' name.

- ***Concentration of Credit Risk –*** An increased risk of loss occurs as more investments are acquired from one issuer which results in a concentration of credit risk. Excluding securities issued by U.S. Government & Agencies, Citizens does not hold any securities from any single issuer that exceeded 5% of the investment portfolio.

- ***Interest Rate Risk –*** Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's fair value. Citizen's measures this risk by using the weighted average maturity method. The Corporation's investment policy requires that the weighted average maturity of the portfolio not exceed three years. This policy takes interest rate reset dates, primarily related to tax-exempt variable rate demand notes and floating rate notes, into consideration. The table that follows reflects the weighted average maturity, without consideration of resets, by security type at December 31, 2011 *(in thousands)*. By not considering interest rate reset dates, the weighted average maturity below appears longer in duration than it would if reset dates had been considered.

NOTE 3 – INVESTMENTS (CONTINUED)

Interest Rate Risk (continued)

	Amortized Cost	Fair Value	Weighted Average Maturity *(in days)*
U.S. Treasury & Agency	$ 3,711,180	$ 3,726,682	717
Municipal bonds	4,022,967	4,065,171	1,589
Corporate and other bonds	3,482,081	3,509,293	824
Mortgage-backed securities	1,049	1,021	1,060
Total	$ 11,217,277	$ 11,302,167	1,064

No other types of investments or securities were held during the year that were sold before year-end.

The table that follows reflects the weighted average maturity, without consideration of resets, by security type at December 31, 2010 *(in thousands)*. By not considering interest rate reset dates, the weighted average maturity below appears longer in duration than it would if reset dates had been considered.

	Amortized Cost	Fair Value	Weighted Average Maturity *(in days)*
U.S. Treasury & Agency	$ 3,677,201	$ 3,679,498	362
Municipal bonds	3,478,382	3,477,354	4,040
Corporate and other bonds	2,389,570	2,405,648	503
Mortgage-backed securities	1,402	1,385	1,425
Total	$ 9,546,555	$ 9,563,885	1,735

No other types of investments or securities were held during the year that were sold before year-end.

- ***Foreign Currency Risk –*** Citizens had no investments with foreign currency risk at December 31, 2011 and 2010, respectively. All investments are settled in U.S. dollars.

NOTE 3 – INVESTMENTS (CONTINUED)

Sources and uses of investment income for the years ended December 31, 2011 and 2010 were as follows *(in thousands)*:

	2011	2010
Income earned		
U.S. Government bonds	$ 19,221	$ 7,502
Bonds exempt from U.S. Tax	35,315	10,718
Other bonds	39,062	11,638
Cash, cash equivalents and short-term investments	6,316	14,322
Total gross investment income earned	99,914	44,180
Capital gains (losses)		
U.S. Government bonds	6,447	552
Bonds exempt from U.S. Tax	2,556	97
Other bonds	8,036	3,150
Cash, cash equivalents and short-term investments	21,824	27,088
Other	-	(3)
Total realized gain ~~(loss)~~ on sales or maturities	38,863	30,884
Market value adjustment	67,557	45,670
Investment expense	(5,321)	(4,090)
Net investment income	$ 201,013	$ 116,644

Fair Value Measurement

The Corporation's estimates of fair value for financial assets and financial liabilities are based on the framework established in the Fair Value Measurements and Disclosures accounting guidance. The framework is based on the inputs used in valuation and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the fair value accounting guidance includes a hierarchy based on whether significant valuation inputs are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The three levels of the hierarchy are as follows:

NOTE 3 – INVESTMENTS (CONTINUED)

Fair Value Measurement (continued)

Level 1 – Quoted Prices in Active Markets for Identical Assets and Liabilities: Citizens has no assets or liabilities measured at fair value in this category.

Level 2 – Significant Other Observable Inputs: This category, for items measured are fair value on a recurring basis, includes bonds which are not exchange-traded. The estimated fair values of these items were determined by independent pricing services using observable inputs.

Level 3 – Significant Unobservable Inputs: Citizens has no assets or liabilities measured at fair value in this category.

	(in thousands)			
Description	Level 1	Level 2	Level 3	Total
Bonds & asset-backed securities:				
U.S. and municipal issues	$ -	$ 7,791,853	$ -	$ 7,791,853
Industrial & miscellaneous	-	3,509,293	-	3,509,293
Loan-backed and structured securities	-	1,021		1,021
Total bonds & asset-backed securities	$ -	$ 11,302,167	$ -	$ 11,302,167

At the end of each reporting period, the Company evaluates whether or not any event has occurred or circumstances have changed that would cause an instrument to be transferred into or out of Level 3. During the current year, no transfers into or out of Level 3 were required. The Company has no assets or liabilities measured at fair value in the Level 3 category.

Bonds carried at fair value categorized as Level 2 are valued using the market approach. The estimated fair values of some of these items were determined by independent pricing services and relevant market data observable inputs. Others were based on broker quotes from markets which were not considered actively traded. Some valuations were determined to be Level 2 valuations as quoted market prices for similar instruments in an active market were utilized. This was accomplished by the use of matrix pricing. Matrix pricing takes quoted prices of bonds with similar features and applies analytic methods to determine the fair value of bonds held. Features that are inputs into the analysis include duration, credit quality, tax status and call and sinking fund features.

NOTE 4 - CAPITAL ASSETS

A summary of changes in capital assets and depreciation for the year ended December 31, 2011 follows *(in thousands)*:

	Beginning Balance	Additions	Reductions/ Adjustments	Ending Balance
Leasehold improvements	$ 7,425	$ 418	$ -	$ 7,843
Furniture and equipment	35,408	2,124	-	37,532
Other capital assets	31,550	125	-	31,675
Totals at historical cost	74,383	2,667	-	77,050
Less accumulated depreciation for:				
Leasehold improvements	(3,255)	(714)	-	(3,969)
Furniture and equipment	(30,168)	(2,826)	-	(32,994)
Other capital assets	(30,151)	(1,102)	-	(31,253)
	(63,574)	(4,642)	-	(68,216)
	$ 10,809	$ (1,975)	$ -	$ 8,834

A summary of changes in capital assets and depreciation for the year ended December 31, 2010 follows *(in thousands)*:

	Beginning Balance	Additions	Reductions/ Adjustments	Ending Balance
Leasehold improvements	$ 7,279	$ 146	$ -	$ 7,425
Furniture and equipment	34,088	1,442	(122)	35,408
Other capital assets	31,479	101	(30)	31,550
Totals at historical cost	72,846	1,689	(152)	74,383
Less accumulated depreciation for:				
Leasehold improvements	(2,561)	(694)	-	(3,255)
Furniture and equipment	(24,901)	(5,313)	46	(30,168)
Other capital assets	(26,713)	(3,445)	7	(30,151)
	(54,175)	(9,452)	53	(63,574)
	$ 18,671	$ (7,763)	$ (99)	$ 10,809

NOTE 5 - LIABILITY FOR LOSS RESERVES AND LOSS ADJUSTMENT EXPENSE RESERVES

Activity in the net liability for loss reserves and loss adjustment expense reserves for the years ended December 31, 2011 and 2010 were as follows *(in thousands)*:

	2011	2010
Direct loss and loss adjustment expense reserves, beginning of year	$ 954,765	$ 887,339
Less reinsurance recoverables on reserves	(98,500)	(145,192)
Net loss and loss adjustment expense reserves, beginning of year	856,265	742,147
Incurred related to:		
Current year	1,236,012	786,224
Prior years	118,824	(23,290)
Total incurred	1,354,836	762,934
Paid related to:		
Current year	501,310	330,603
Prior years	363,221	318,213
Total paid	864,531	648,816
Net loss and loss adjustment expense reserves, end of year	1,346,570	856,265
Add reinsurance recoverable on reserves	26,076	98,500
Direct loss and loss adjustment expense reserves, end of year	$ 1,372,646	$ 954,765

As a result of changes in estimates of insured events in prior years, primarily due to the estimation of costs relating to prior year hurricane claims, the provision for loss and loss adjustment expenses increased by approximately $118.8 million and decreased by approximately $23.3 million, net of reinsurance, in 2011 and 2010, respectively. Increases or decreases of this nature occur as a result of claim settlements during the current year, and as additional information is received regarding individual claims, causing changes from the original estimates of the cost of these claims. The increase in 2011 loss and LAE reserves is largely due to the Hurricane Wilma commutation with the FHCF and increases in overall exposure and frequency. The losses and LAE incurred increase is largely attributable to an increase in the amount of sinkhole claims being reported in 2011 for both prior accident periods as well as the current accident period.

For both catastrophic and non-catastrophic claims, the loss adjusting function is performed by Citizens through its employees and through contracted independent adjusting firms. Citizens compensates independent adjusting firms, depending upon the type or nature of the claims, either

NOTE 5 - LIABILITY FOR LOSS RESERVES AND LOSS ADJUSTMENT EXPENSE RESERVES (CONTINUED)

on per-day rate or on a graduated fee schedule based on the gross claim amount, consistent with industry standard methods of compensation. Such costs are included as loss adjustment expenses.

NOTE 6 - REINSURANCE AGREEMENTS

Citizens participates in the Florida Hurricane Catastrophe Fund. The FHCF will reimburse Citizens a specified percentage of losses incurred relating to a hurricane in Florida if a prescribed retention is reached subject to a maximum limit. Premiums ceded to the FHCF, net of refunds received, totaled $453.1 million and $368.1 million, during 2011 and 2010 respectively. The Coastal Account is treated for all FHCF purposes as if it were a separate participating insurer with its own exposures, reimbursement premium and loss reimbursement. Likewise, the Personal and Commercial Lines Accounts are viewed together for FHCF purposes, as if the two accounts were one and represent a single, separate participating insurer with its own exposures, reimbursement premium and loss reimbursement. The FHCF coverages and retention amounts by account are as follows *(in thousands)*:

	2011		2010	
	Coverage Amounts	Retention Amounts	Coverage Amounts	Retention Amounts
Personal and Commercial Lines accounts	$ 2,769,346	$ 1,162,377	$ 2,143,144	$ 866,667
Coastal account	3,919,866	1,645,285	3,750,451	1,516,646

Citizens purchased private reinsurance for the Coastal Account in 2011. The private reinsurance will reimburse Citizens a specified percentage of losses incurred relating to hurricanes in Florida if a prescribed retention is reached. Reinsurance is on a per occurrence basis. Premiums ceded to private reinsurers, net of refunds received, totaled $113.6 million during 2011. Citizens did not purchase private reinsurance in 2010. The private reinsurance coverages and retention amount by account were as follows *(in thousands)*:

	2011	
	Coverage Amounts	Retention Amounts
Coastal account	$ 575,000	$ 6,302,000

NOTE 6 - REINSURANCE AGREEMENTS (CONTINUED)

The effect of reinsurance on premiums written and earned is as follows *(in thousands)*:

	2011		2010	
	Written	Earned	Written	Earned
Direct	$ 3,084,342	$ 2,853,665	$ 2,604,265	$ 2,393,150
Ceded	(611,207)	(601,934)	(389,833)	(421,501)
Net premiums	$ 2,473,135	$ 2,251,731	$ 2,214,432	$ 1,971,649

Premium ceded above also includes premium ceded to companies that assume policies pursuant to a depopulation program (See Note 12).

During 2011, Citizens entered into a commutation agreement with the FHCF regarding the Hurricane Wilma losses and LAE. Pursuant to the agreement, Citizens received payment of $41.3 million in exchange for assuming outstanding reserves equal to $56.2 million. The net effect of the agreement resulted in the recognition of $14.9 million in additional incurred losses and LAE.

In addition, Citizens is entitled to $47.4 million in private reinsurance reimbursements in the Coastal Account related to losses incurred and paid as a result of Hurricane Wilma in 2005. Citizens is also entitled to $95.8 million in private reinsurance reimbursement in the Personal Lines Account related to losses incurred and paid as a result of all four hurricanes (Dennis, Katrina, Rita and Wilma) in 2005. FHCF recoveries of $1.0 billion and private reinsurance recoveries of $140.0 million were received as of December 31, 2011.

Amounts recoverable from reinsurers on unpaid losses and loss adjustment expenses are estimated based on the allocation of estimated unpaid losses and loss adjustment expenses among Citizens' coverage lines. Actual amounts recoverable will depend on the ultimate settlement of losses and loss adjustment expenses. Reinsurance contracts do not relieve Citizens from its obligation to policyholders. Citizens remains liable to its policyholders for the portion reinsured to the extent that any reinsurer does not meet the obligations assumed under their reinsurance agreements.

NOTE 7 – LONG-TERM DEBT

Series 2007A Senior Secured Refunding Bonds - On February 26, 2007 Citizens issued $1.06 billion of tax exempt post event High-Risk Account Senior Secured Refunding Bonds, Series 2007A at a premium of $60.1 million for the purpose of financing the current refunding and redemption of the outstanding 7.125% Series 1999A Senior Secured Insured Notes due 2019 previously issued by the FWUA. In order to refund these notes Citizens paid a make whole call premium at the time of refunding, amounting to $181.1 million that was calculated on the current yield of a 12 year treasury note plus 30 basis points. The 2007A bonds bear interest ranging from 3.75% to 5.00% per annum, payable semi-annually on March 1st and September 1st. The

NOTE 7 – LONG-TERM DEBT (CONTINUED)

bonds are secured by pledged revenues which consist of monies and investments held in accounts established under the trust indenture, proceeds from any regular assessment and/or reimbursements received from the FHCF. The bond maturity dates range from March 1, 2008 to March 1, 2017. The principal reduction on these notes was $100.9 million and $96.2 million during 2011 and 2010, respectively. Outstanding maturities, including unamortized premiums and discounts were $741.7 million and $849.6 million, respectively, as of December 31, 2011 and 2010.

Series 2008 Senior Secured Bonds **–** On June 30, 2008 Citizens issued $250 million of High-Risk Account tax-exempt senior secured bonds, Series 2008A-1 and $1.5 billion of High-Risk Account tax-exempt senior secured bonds, Series 2008A-2 (short-term notes) for the purpose of funding losses in the event of a future catastrophe. The bonds bear interest ranging from 4.50% to 5.00% per annum, payable semi-annually on June 1st and December 1st. The bonds are secured by pledged revenues which consist of monies and investments held in accounts established under the trust indenture, proceeds from any regular assessment and/or reimbursements received from the FHCF. The bond maturity dates range from June 1, 2009 to June 1, 2011. The principal reduction on these notes was $250 million and $0 during 2011 and 2010, respectively. Outstanding maturities, including unamortized premiums were $0 and $250.6 million, respectively, as of December 31, 2011 and 2010.

Series 2009 Senior Secured Bonds **–** On May 7, 2009 Citizens issued $1.02 billion of High-Risk Account tax-exempt senior secured bonds, Series 2009A-1 and $625 million of High-Risk Account tax-exempt senior secured bonds, Series 2009A-2 (short-term notes) for the purpose of funding losses in the event of a future catastrophe. The Series 2009A-1 bonds bear interest ranging from 4.00% to 6.00% per annum, payable semi-annually on June 1st and December 1st. The Series 2009A-2 bonds bear interest of 4.50% per annum, payable on May 1, 2010 and on June 1, 2010. The bonds are secured by pledged revenues which consist of monies and investments held in accounts established under the trust indenture, proceeds from any regular assessment and/or reimbursements received from the FHCF. The bond maturity dates range from June 1, 2009 to June 1, 2017. The principal reduction on these notes was $0 and $625.0 million during 2011 and 2010, respectively. Outstanding maturities, including unamortized premiums and discounts were $1.03 billion and $1.03 billion, respectively, as of December 31, 2011 and 2010.

Series 2010 Senior Secured Bonds **-** On April 6, 2010 Citizens issued $1.55 billion of High-Risk Account tax-exempt senior secured bonds, Series 2010A-1, $500 million of High-Risk Account tax-exempt senior secured bonds, Series 2010A-2 (short-term notes) and $350 million of High-Risk Account tax-exempt senior secured bonds, Series 2010A-3 (Securities Industry and Financial Markets Association (SIFMA) floating rate notes) for the purpose of funding losses in the event of a future catastrophe. The Series 2010A-1 bonds bear interest ranging from 3.00% to 5.00% per annum, payable semi-annually on June 1st and December 1st. The Series 2010A-2 bonds bear interest of 2.00% per annum, payable at their maturity on April 21, 2011. The Series 2010A-3 bonds have a variable interest rate (SIFMA rate plus 1.75%) per annum, payable monthly in arrears on the first day of each calendar month. The bonds are secured by pledged

NOTE 7 – LONG-TERM DEBT (CONTINUED)

revenues which consist of monies and investments held in accounts established under the trust indenture, proceeds from any regular assessment and/or reimbursements received from the FHCF. The principal reduction on these notes was $500 million and $0 during 2011 and 2010, respectively. Outstanding maturities net of unamortized premiums and discounts were $1.95 billion and $2.47 billion, as of December 31, 2011 and 2010.

Series 2011 Senior Secured Bonds - On July 14, 2011 Citizens issued $645 million of Coastal Account tax-exempt senior secured bonds, Series 2011A-1, $105 million of Coastal Account tax-exempt senior secured bonds, Series 2011A-2 (short-term notes) and $150 million of Coastal Account tax-exempt senior secured bonds, Series 2011A-3 (SIFMA floating rate notes) for the purpose of funding losses in the event of a future catastrophe. The Series 2011A-1 bonds bear interest ranging from 3.00% to 5.00% per annum, payable semi-annually on June 1st and December 1st. The Series 2011A-2 bonds bear interest of 2.00% per annum, payable at their maturity on June 1, 2012. The Series 2011A-3 bonds bear interest based on the SIFMA rate (initially 0.11%) plus 1.65% per annum, payable monthly in arrears on the first day of each calendar month. The bonds are secured by pledged revenues which consist of monies and investments held in accounts established under the trust indenture, proceeds from any regular assessment and/or reimbursements received from the FHCF. There were no principal reductions on these notes during 2011. Outstanding maturities net of unamortized premiums and discounts were $922.5 million as of December 31, 2011.

A schedule of bond maturities is as follows *(in thousands)*:

Year ending December 31	Series 2007 Bonds	Series 2009 Bonds	Series 2010 Bonds	Series 2011 Bonds	Total
2012	$ 106,125	$ 106,360	$ -	$ 105,000	$ 317,485
2013	111,530	-	560,000	-	671,530
2014	117,220	168,055	100,000	150,000	535,275
2015	123,225	-	410,000	80,000	613,225
2016	129,540	403,085	305,000	90,000	927,625
After	136,165	343,500	525,000	475,000	1,479,665
Total	$ 723,805	$ 1,021,000	$ 1,900,000	$ 900,000	$ 4,544,805

NOTE 7 – LONG-TERM DEBT (CONTINUED)

A schedule of debt service requirements, including principal and interest, is as follows *(in thousands)*:

Year ending December 31	Principal	Interest	Total
2012	$ 317,485	$ 203,685	$ 521,170
2013	671,530	185,683	857,213
2014	535,275	162,837	698,112
2015	613,225	135,584	748,809
2016	927,625	94,163	1,021,788
After	1,479,665	79,004	1,558,669
Total	$ 4,544,805	$ 860,956	$ 5,405,761

Unamortized premium at December 31, 2011 and 2010 was $98.5 million and $101.2 million, respectively.

Total deferred issuance costs related to all notes was $106.6 million and $124.2 million at December 31, 2011 and 2010 and is included in "Deferred financing costs" in the Statements of Net Assets. Total bond premium related to all notes was $98.5 million and $101.2 million at December 31, 2011 and 2010 and is also included in "Long-term debt" in the Statements of Net Assets.

A summary of changes in long-term liabilities for the year ended December 31, 2011 follows *(in thousands)*:

	12/31/2010	Additions	Reductions	12/31/2011	Due within one year
Bonds payable - face	$4,495,800	$ 900,000	$ (850,995)	$4,544,805	$ 344,720
Premium, net	101,200	24,940	(27,629)	98,511	(27,235)
Bonds payable	$4,597,000	$ 924,940	$ (878,624)	$4,643,316	$ 317,485

NOTE 7 – LONG-TERM DEBT (CONTINUED)

Sources and uses of investment expense for the years ended December 31, were as follows *(in thousands)*:

Interest expense	2011	2010
2007A Bond Series	$ (30,031)	$ (33,927)
2008A Bond Series	(4,566)	(11,006)
2009A Bond Series	(54,615)	(69,517)
2010A Bond Series	(70,380)	(56,895)
2011A Bond Series	(14,485)	-
Other prior year interest expense	1,155	-
Change in deferral - loss on refunding of 1999 bonds	(16,721)	(16,721)
Total interest expense	$ (189,643)	$ (188,066)

Interest Rate Swap Agreements – Citizens had no interest rate exchange agreements outstanding at December 31, 2011 and 2010.

NOTE 8 - AGENT COMMISSIONS AND SERVICING COMPANY FEES

Citizens has contracted with various insurance agents licensed in the State of Florida. These agreements provide for commissions to be paid to the agents at rates established by the Board and calculated as a percentage of direct written premiums, net of certain surcharges and assessments. Agent commissions were $230.9 million and $193.5 million during 2011 and 2010, respectively.

Additionally, Citizens entered into an agreement with a servicing company to provide underwriting and policy management services. The agreement provides for monthly compensation to the company based on a “Per Transaction Fee” applied to the number of transactions processed in a monthly cycle. During 2010, Citizens and the servicing company entered a new contract effective October 1, 2010, that continues through September 30, 2013, for services similar to those being performed previously. These services are for both Citizens’ Commercial Lines and Personal Lines business. The amount per transaction ranges from $3.50 to $50.00, depending on the complexity and volume of each transaction. Service company fees were $9.3 million and $8.3 million, during 2011 and 2010, respectively.

NOTE 9 - INCOME TAXES

Pursuant to a determination letter received from the Internal Revenue Service, Citizens is exempt from federal income tax as a political subdivision and integral part of the State of Florida and as such, is liable for income taxes only on business income unrelated to the purpose for which it is exempt. No federal or state income tax was incurred in 2011 or 2010.

NOTE 10 - LINE OF CREDIT AGREEMENTS

Effective May 7, 2009, Citizens entered into a $400 million credit agreement (the 2009 PLA/CLA Line of Credit) with a syndication of banks to pay claims and liabilities and expenses related to claims under the Personal and Commercial Lines Accounts. The 2009 Line of Credit is secured by a security interest in anticipation of revenues consisting of FHCF reimbursements and/or regular assessments, including additional surcharges or assessments. Citizens is required to pay an annual facility fee of 1.4% on the unused portion of the facility. This rate is based on ratings by Moody's Investor Service, Inc. and Standard and Poor's Ratings Services (S&P) of A-/A3 or better, on Personal and Commercial Lines Accounts long-term debt. The current PLA/CLA ratings are A2/A+ from Moody's and S&P, respectively. Unused facility fee expenses associated with this credit agreement was $1.96 million for the year ended December 31, 2010. The agreement expired on May 6, 2010 and was not renewed.

NOTE 11 - RETIREMENT PLAN

Deferred Compensation Plan

Citizens sponsors a 457(b)/401(a) defined contribution employee savings plan for qualified employees (the Savings Plan). The Savings Plan qualifies as a deferred salary arrangement under Section 401(a) of the Internal Revenue Code. Under the Savings Plan, participating eligible employees may defer a portion of their pretax earnings, up to the Internal Revenue Service annual contribution limit. Citizens matches 100% of each employee's contributions, up to a maximum of 8% of the employee's pretax earnings. Citizens' matching contributions to the Savings Plan were $3.4 million and $2.9 million for the years ended December 31, 2011 and 2010, and are included in "Other underwriting expenses" in the accompanying Statements of Revenues, Expenses and Changes in Net Assets.

NOTE 12 - DEPOPULATION

Pursuant to the Act, Citizens is authorized to adopt one or more programs, subject to approval by the Office, for the reduction of both new and renewal writings. Both of the pre-merger entities, the FRPCJUA and the FWUA, were also authorized to adopt and did enact such programs. However, the FRPCJUA was the only entity authorized to pay bonuses related to such programs. Agreements were entered into with various insurance companies (the Takeout Company or Companies) licensed in the State of Florida to remove policies from the FRPCJUA or the FWUA.

Policies may be removed from Citizens at policy renewal or as part of a bulk assumption (Assumption Agreement). In an assumption, the Takeout Company is responsible for losses occurring from the assumption date through the expiration of the Citizens' policy period (the assumption period). Subsequent to the assumption period, the Takeout Company will write the policy directly. In January 2007, Florida law was amended to state that assumed policies are the direct insurance of the Takeout Company, for the purpose of clarifying that FIGA is liable for assumption period losses occurring during the assumption period if a Takeout Company were liquidated and unable to meet its obligation to policyholders.

NOTE 12 – DEPOPULATION (CONTINUED)

During 2011 and 2010, Citizens ceded $44.5 million and $21.8 million in premiums to Takeout Companies pursuant to Assumption Agreements which is included in "Premiums earned" in the accompanying Statements of Revenues, Expenses and Changes in Net Assets.

Citizens provides policy administration services with respect to the assumed policies. All agreements provide for the Takeout Company to adjust losses. The Takeout Company pays a ceding commission to Citizens to compensate Citizens for policy acquisition costs, which includes servicing company fees, agent commissions, and premium taxes. However, In February 2012, Citizens Board of Governors eliminated the ceding commission for all assumption agreements effective after October 1, 2011. While Citizens is not liable to cover claims after the assumption (unless it allows the insured to return to Citizens for coverage), Citizens continues to service policies for items such as policyholder endorsements or cancellation refunds. Should Citizens process and provide a refund to policyholders, such amount is subsequently collected from the Takeout Company. At December 31, 2011 and 2010, assumed premiums recoverable in the amount of $0.9 million and $3.1 million were due from certain Takeout Companies.

Certain agreements provide for a policy takeout bonus of up to 25% of annual policy premium to be paid to the Takeout Companies. Such takeout bonuses have been placed into escrow bank accounts pursuant to an escrow agreement. After a specific time period, funds placed in escrow will be released to the Takeout Companies in accordance with the policy takeout agreement.

During 2011 and 2010, Citizens paid $4.7 million and $0, respectively, out of escrow (net of certain recoveries). During 2011 and 2010, Citizens paid $0 into escrow in accordance with the policy takeout agreements for policies removed. Citizens has not had a takeout bonus policy in effect since the 2007 depopulation programs. In 2011 and 2010 respectively, 53,577 and 59,792 policies were removed from Citizens pursuant to its depopulation program.

At the end of the applicable time period, Citizens requires the Takeout Companies to have an independent audit of the policies for which they are claiming a bonus to determine if the policy is properly classified and is eligible for payment of the bonus, if any. Based upon results of that audit, Citizens evaluates the original amounts placed into escrow to determine if the escrow account is over or underfunded. During 2011 and 2010, Citizens paid into escrow $0 for underfunded accounts and recovered $4.3 million and $0.13 million, respectively, for overfunded accounts. These amounts are included in "Takeout bonus (income) expense" in the accompanying Statements of Revenues, Expenses and Changes in Net Assets.

NOTE 13 - OPERATING LEASES

Citizens leases office space and certain office equipment under various operating leases. Rental expense on operating leases amounted to $6.9 million and $7.1 million for the years ended December 31, 2011 and 2010. At December 31, 2011, future minimum payments under operating leases are as follows (in thousands):

2012	$ 5,511
2013	4,137
2014	2,827
2015	2,062
2016	1,456
After	913
Total	$ 16,906

NOTE 14 - COMMITMENTS AND CONTINGENCIES

Citizens has been informed that the Securities and Exchange Commission, the Florida Office of Financial Regulation, the State of New York Office of the Attorney General Bureau of Investor Protection and the Texas State Securities Board (collectively, the "Agencies") have opened inquiries or investigations of Citizens' purchase of its own auction rate securities in early 2008. Citizens is voluntarily cooperating with the Agencies and is of the belief that any action, if any, by one or more of the Agencies will not materially affect the financial condition of Citizens.

Citizens is involved in certain litigation and disputes incidental to its operations. In the opinion of management, after consultation with legal counsel, there are substantial defenses to such litigation and disputes and any ultimate liability, in excess of reserves resulting there from, will not have a material adverse effect on the financial condition or results of operations of Citizens.

Citizens is also involved in other potentially significant litigation described below. Due to the preliminary nature of the following litigation, the potential loss, if any, is not determinable at this time.

A summary of potentially significant litigation follows:

<u>Poe & Associates, L.L.C. (Associates) v. Citizens</u>. This lawsuit relates to Citizens' June 2006 termination of its agent appointment agreement with Associates, thereby preventing Associates from being able to receive future commissions on policies that Citizens issued to former policyholders of insolvent insurance companies affiliated with Associates and owned by Poe Financial Group, Inc. Associates seek significant damages. Its many claims include breach of contract, tortuous interference, and regulatory taking. Citizens believes it will ultimately prevail on all claims presented.

NOTE 14 - COMMITMENTS AND CONTINGENCIES (CONTINUED)

Schirmer v. Citizens. This case was presented as a putative class action where the potential class members are Citizens' policyholders who made wind damage claims. At issue is whether Citizens appropriately calculated and paid overhead and profit policy benefits. On February 15, 2012 the trial court declined to certify a class in this matter. While the 30 day timeframe for the Plaintiff to pursue an interlocutory appeal of the court's decision has passed, the underlying claim of the named Plaintiff is pending. Should the Plaintiff choose to litigate his remaining claim, he could seek appellate review at the conclusion of the matter in its entirety.

Davis & Hernandez v. Citizens. This is a putative class action. The court has not certified the class. Potential class members are Citizens' policyholders who presented a claim for damage to their residential property from April 2006 to present. At issue is whether Citizens appropriately calculated and paid overhead and profit policy benefits.

Citizens v. San Perdido. Citizens appealed the trial court's ruling that Citizens does not have sovereign immunity for a cause of action of statutory bad faith pursuant to Section 624.155, Florida Statutes, to the 1st District Court of Appeals (DCA). The 1st DCA issued an opinion in conflict with the prior favorable ruling from the 5th DCA in *Garfinkel v. Citizens, 2009 WL 4874789 (Fla.App. 5 Dist., finding Citizens immune from a statutory bad faith action).* This matter is currently on appeal to the Florida Supreme Court due to a conflict between the districts courts of appeal.

During the first quarter of 2012, the Company was served on a lawsuit relating to the Company's use of its replacement cost estimator. The case is styled *Joe Freitas v. Citizens Property Insurance Corporation and Xactware Solutions, Inc.* and is filed in the Pasco County Circuit Court. The action is brought by the plaintiff, individually and on behalf of a class of all persons similarly situated. To date, a class has not been certified in this action. At this time, the Company cannot estimate the likelihood of a favorable or unfavorable outcome nor can the Company estimate a potential liability, if any.

Additionally in the first quarter of 2012, the Company was served on a lawsuit relating to the Company's use of certain Inspection Forms and subsequently requiring insureds to undergo home re-inspections. The case is styled *Kenneth Babbitt, Katherine Livesay and Others v. Citizens Property Insurance Corporation* and is filed in Broward County Circuit Court. The action is brought by the plaintiffs, individually and on behalf of a class of all persons similarly situated. To date, a class has not been certified in this action. At this time, the Company cannot estimate the likelihood of a favorable or unfavorable outcome nor can the Company estimate a potential liability, if any.

Risk Management Programs

In addition to claims under the insurance policies it issues, Citizens is potentially exposed to various risks of loss, including those related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. As a state government entity, Citizens has immunity from certain claims. As of the end of 2011, Citizens had insurance

NOTE 14 - COMMITMENTS AND CONTINGENCIES (CONTINUED)

Risk Management Programs (Continued)

protection in place from various commercial insurance carriers covering various exposures, including workers' compensation, property loss, employee liability, general liability, and directors and officers' liability. Management continuously reviews the limits of coverage and believes that current coverage is adequate. There were no significant reductions in insurance coverage from the previous year.

NOTE 15 - RECONCILIATION OF SAP TO GAAP

Reconciliation of Citizens' 2011 and 2010 statutory basis net income and accumulated surplus to its GAAP basis (as determined by the Governmental Accounting Standards Board) net assets is as follows *(in thousands)*:

	2011	2010
Net income - statutory basis	$ 448,701	$ 744,729
Adjustments:		
Deferred policy acquisition costs	14,300	33,270
Line of credit fees and note issuance costs	(17,628)	(10,126)
Takeout bonuses	-	(1,722)
Allowance for doubtful accounts	690	415
Unearned assessment income	21,620	21,183
Unrealized gain on investments	67,557	45,670
Change in net assets - GAAP basis	$ 535,240	$ 833,419

	2011	2010
Accumulated surplus - statutory basis	$ 5,588,141	$ 5,101,534
Adjustments:		
Deferred policy acquisition costs	144,947	130,647
Nonadmitted assets	147,446	181,779
Provision for reinsurance	2,664	5,665
Deferred note issuance costs	106,580	124,208
Unearned assessment income	(39,876)	(61,496)
Net unrealized gain on investments	84,890	17,333
Total net assets - GAAP basis	$ 6,034,792	$ 5,499,670

NOTE 16 - ASSESSMENTS

Citizens' enabling legislation and the Plan establish a process by which Citizens is required to levy assessments to recover deficits incurred in a given plan year for any of its three accounts. Deficits are calculated separately, and assessments are accordingly levied separately, for each of the three accounts. The Plan provides for deficits to be determined in accordance with GAAP, adjusted for certain items.

In the event of a Plan Year Deficit in any Account, Citizens must first levy an assessment against the premium of each Citizens policyholder (the "Citizens Policyholder Surcharge") in each of Citizens' Accounts, as a uniform percentage of the premium of the policy of up to 15% of such premium. Citizens Policyholder Surcharges are not subject to commissions, fees, or premium taxes; however, failure to pay a Citizens Policyholder Surcharge will be treated as failure to pay premiums. If the Citizens Policyholder Surcharge is insufficient to eliminate the deficit in an Account, Citizens would then levy a Regular Assessment on Assessable Insurers and Assessable Insureds, each as defined herein. The Regular Assessment is applied as a uniform percentage of the premium of the policy up to 6% of such premium per account.

Regular Assessments are levied on Assessable Insurers, as defined in Section 627.351(6), Florida Statutes, based upon each Assessable Insurer's share of direct written premium for the subject lines of business in the State of Florida for the calendar year preceding the year in which the deficit occurred. Regular Assessments on Assessable Insureds, collectively, are based on the ratio of the amount being assessed for an Account to the aggregate statewide direct written premiums for the subject lines of business for the preceding year.

If the deficit in any year in any Account is greater than the amount that may be recovered through Citizens' Policyholder Surcharges and Regular Assessments, Citizens is required to levy any remaining Plan Year Deficit as an Emergency Assessment. An Emergency Assessment is to be collected by all Assessable Insurers, Surplus Lines Agents and Citizens from policyholders upon the issuance or renewal of policies for Subject Lines of Business for as many years as necessary to cover the Plan Year Deficit in the Account. The primary difference between the assessment base for Regular Assessments and Emergency Assessments is the inclusion of Citizens' direct written premium in the assessment base for Emergency Assessments.

For purposes of Regular Assessments and Emergency Assessments, the "Subject Lines of Business" are all lines of property and casualty insurance, including automobile lines, but excluding accident and health, workers' compensation, and medical malpractice insurance, and also excluding insurance under the National Flood and Federal Crop insurance programs. The Regular Assessment base excludes Citizens policies (while the Emergency Assessment base includes Citizens policies). Prior to the enactment of the 2007 Legislation, the Regular Assessment base for each Account included only property lines of business.

The Legislature, in Section 44 of 2006 SB 1980, appropriated $715 million to reduce Citizens' 2005 plan year deficit. The appropriation first eliminated the deficits in the Personal and Commercial Lines Accounts of $87.2 million and $4.6 million, respectively. The balance of $623.3 million then partially reduced the High Risk Account deficit and Regular Assessment.

NOTE 16 – ASSESSMENTS (CONTINUED)

The remaining $163.1 million High Risk Account Regular Assessment and the $887.5 million Emergency Assessment were approved in 2006. The Emergency Assessment is being collected over a ten year period which commenced July 1, 2007.

NOTE 17 - RESTRICTED CASH

This restriction of cash surplus represents assessments that were, in accordance with the Act, over-collected by the Florida Surplus Lines Servicing Office (FSLSO) from surplus lines insureds with respect to the 2004 Plan Year Deficit. Pursuant to a consent order, the Office, FSLSO and Citizens agreed that this cash would be included in Citizens restricted surplus until such time future regular and emergency assessments would otherwise be payable by surplus lines insureds. As amounts have been approved by FSLSO with respect to regular and emergency assessments for Citizens' 2005 Plan Year deficit, Citizens has transferred these funds to unrestricted surplus.

Citizens Property Insurance Corporation
Supplemental Combining Statement of Net Assets

	December 31, 2011			
	Combined	Personal Lines Account	Commercial Lines Account	Coastal Account
	(In Thousands)			
Assets				
Current assets:				
Cash and cash equivalents	$ 1,575,852	$ 467,120	$ 81,236	$ 1,027,496
Short-term investments	1,999,099	512,977	130,875	1,355,247
Restricted cash and cash equivalents	11,726	-	-	11,726
Deferred policy acquisition costs	144,947	75,121	12,553	57,273
Investment income due & accrued	72,831	14,063	5,856	52,912
Prepaid reinsurance premiums	25,889	22,450	-	3,439
Reinsurance recoverable on paid losses and LAE	3,130	2,696	-	434
Premiums receivable	181,018	102,651	6,134	72,233
Premiums receivable from assuming companies	874	811	-	63
Current portion of deferred financing costs	22,795	-	-	22,795
Current portion of assessment receivables	89,948	(762)	4,624	86,086
Total current assets	4,128,109	1,197,127	241,278	2,689,704
Noncurrent assets:				
Long-term investments	9,303,068	2,539,015	1,266,415	5,497,638
Deferred takeout bonus	-	-	-	-
Capital assets	8,834	8,834	-	-
Deferred financing costs	83,785	-	-	83,785
Assessment receivables	391,354	-	-	391,354
Other assets	8,838	8,801	3	34
Inter-account receivable (payable)	-	31,195	(11,483)	(19,712)
Total noncurrent assets	9,795,879	2,587,845	1,254,935	5,953,099
Total assets	$ 13,923,988	$ 3,784,972	$ 1,496,213	$ 8,642,803
Liabilities and net assets				
Current liabilities:				
Loss reserves	$ 1,093,917	$ 810,264	$ 127,658	$ 155,995
Loss adjustment expense reserves	252,653	185,160	26,145	41,348
Unearned premiums	1,437,120	820,145	93,834	523,141
Current portion of unearned assessment income	48,881	-	-	48,881
Reinsurance premiums payable	55,684	-	-	55,684
Advance premiums and suspended cash	99,291	50,813	7,510	40,968
Interest payable	27,479	-	-	27,479
Taxes and fees payable	6,477	4,909	753	815
Current portion of long-term debt	317,485	-	-	317,485
Other current liabilities	116,669	80,372	4,712	31,585
Total current liabilities	3,455,656	1,951,663	260,612	1,243,381
Noncurrent liabilities:				
Unearned assessment income	107,709	-	-	107,709
Long-term debt	4,325,831	-	-	4,325,831
Total noncurrent liabilities	4,433,540	-	-	4,433,540
Total liabilities	7,889,196	1,951,663	260,612	5,676,921
Net assets:				
Invested in capital assets	8,834	8,834	-	-
Restricted	11,726	-	-	11,726
Unrestricted	6,014,232	1,824,475	1,235,601	2,954,156
Total net assets	6,034,792	1,833,309	1,235,601	2,965,882
Total liabilities and net assets	$ 13,923,988	$ 3,784,972	$ 1,496,213	$ 8,642,803

See independent auditors report on supplementary information

Citizens Property Insurance Corporation
Supplemental Combining Statement of Revenues, Expenses, and Changes in Net Assets

	Year Ended December 31, 2011			
	Combined	Personal Lines Account	Commercial Lines Account	Coastal Account
		(In Thousands)		
Operating revenue:				
Premiums earned	$ 2,251,731	$ 1,311,333	$ 172,624	$ 767,774
Operating expenses:				
Losses incurred	1,107,600	960,886	11,180	135,534
Loss adjustment expenses incurred	247,236	186,488	6,181	54,567
Service company fees	9,317	6,443	-	2,874
Agent commissions	230,926	103,792	23,278	103,856
Taxes and fees	45,419	24,590	3,413	17,416
Processing and other fees	1,403	-	1,205	198
Other underwriting expenses	146,980	81,624	8,616	56,740
Takeout bonus expense (income)	(4,254)	(4,254)	-	-
Total operating expenses	1,784,627	1,359,569	53,873	371,185
Operating income	467,104	(48,236)	118,751	396,589
Nonoperating revenues (expenses):				
Net investment income	201,013	51,145	29,038	120,830
Interest expense	(189,643)	-	-	(189,643)
Assessment income	56,941	-	-	56,941
Line of credit fees and note issuance costs	(6,915)	-	-	(6,915)
Other income	6,740	4,818	862	1,060
Total nonoperating revenues (expenses)	68,136	55,963	29,900	(17,727)
Change in net assets	535,240	7,727	148,651	378,862
Net assets, beginning of year	5,499,670	1,825,582	1,086,950	2,587,138
Other changes in net assets	(118)	-	-	(118)
Net assets, end of year	$ 6,034,792	$ 1,833,309	$ 1,235,601	$ 2,965,882

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Citizens Property Insurance Corporation
Supplemental Revenues, Expenses, and Claim Development Information
(in Thousands)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Net earned premiums and investment revenue	$ 754,581	$ 929,691	$ 1,129,092	$ 1,143,973	$ 2,289,760	$ 3,417,277	$ 2,268,368	$ 1,822,227	$ 2,088,293	$ 2,452,744
Unallocated expenses	283,265	150,578	191,333	227,795	321,522	569,661	442,570	342,840	293,047	366,109
Estimated incurred claims and expense, end of policy year	97,373	243,767	2,721,512	2,138,004	339,770	692,583	839,708	674,431	786,223	1,236,012
Paid (cumulative) as of:										
End of policy year	44,863	123,943	1,145,602	1,005,020	157,640	353,312	413,175	307,072	330,603	501,310
One year later	77,758	200,635	2,952,024	2,114,174	291,045	555,540	622,104	472,476	553,965	
Two years later	82,694	215,997	3,234,575	2,227,283	326,997	625,868	675,168	532,779		
Three years later	85,512	222,743	3,377,401	2,286,765	341,906	661,758	698,220			
Four years later	86,402	224,527	3,459,449	2,328,746	350,721	677,041				
Five years later	86,738	225,999	3,515,881	2,350,722	355,658					
Six years later	87,041	226,467	3,548,759	2,373,190						
Seven years later	87,140	226,622	3,562,464							
Eight years later	87,144	226,750								
Nine years later	87,124									
Reestimated incurred claims and expense:										
End of policy year	97,373	243,767	2,721,512	2,138,004	339,770	692,583	839,708	674,431	786,223	1,236,012
One year later	87,937	222,519	3,285,721	2,205,877	354,194	678,130	753,244	651,058	876,415	
Two years later	87,011	227,916	3,539,287	2,374,726	359,950	693,332	750,380	624,955		
Three years later	88,085	227,956	3,546,902	2,406,456	358,122	697,792	738,966			
Four years later	87,365	227,454	3,615,254	2,413,674	360,230	701,651				
Five years later	87,188	228,178	3,588,748	2,406,633	360,996					
Six years later	87,200	227,770	3,593,577	2,476,606						
Seven years later	87,225	227,200	3,584,632							
Eight years later	87,144	227,092								
Nine years later	87,747									
Increase (decrease) in estimated incurred claims and expense from end of policy year	603	(108)	(8,945)	69,973	766	3,859	(11,414)	(26,103)	90,192	–

See independent auditors report on supplementary information

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Board of Governors and Management
Citizens Property Insurance Corporation

We have audited the basic financial statements of Citizens Property Insurance Corporation (Citizens), a component unit of the State of Florida, as of and for the year ended December 31, 2011 and have issued our report thereon dated May 21, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of Citizens Property Insurance Corporation is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Citizens Property Insurance Corporation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Citizens Property Insurance Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Citizens Property Insurance Corporation's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Citizens property Insurance Corporation's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

This report is intended solely for the information and use of management, the Board of Govenors, others within the entity, and Auditor General of the State of Florida and is not intended to be and should not be used by anyone other than these specified parties.

Johnson Lambert & Co. LLP

Jacksonville, Florida
May 21, 2012