

Citizens Property Insurance Corporation

Financial Statements

December 31, 2008 and 2007

Citizens Property Insurance Corporation
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December 31, 2008 and 2007

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Independent Auditors' Report

The Board of Governors and Management
Citizens Property Insurance Corporation
Tallahassee, FL

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, 2008 and 2007, 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.

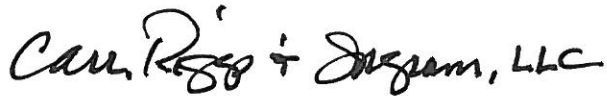
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan 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, 2008 and 2007, 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 April 15, 2009 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 statement 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 supplementary information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink that reads "Carr, Riggs & Ingram, LLC". The signature is written in a cursive, flowing style.

Carr, Riggs & Ingram, LLC
April 15, 2009

Citizens Property Insurance Corporation

Management's Discussion & Analysis

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 \$3.7 billion, increasing the net asset position.
- The Company's total net assets increased by \$638.8 million. This increase is primarily attributable to net income generated as explained below.
- Operating revenues decreased 27% from 2007 to 2008 primarily due to the significant reduction in the number of policies in force, coupled with a lower average premium.
- Operating expenses were reduced by 5% from 2007 to 2008. As written premiums have decreased, so have certain operating expenses that are percentages of written premiums, such as producer commissions, premium taxes and assessments. However, this decrease was significantly offset by an increase in administrative expenses due largely to a continued build out of infrastructure, including the hiring of additional personnel.
- Nonoperating revenues decreased from 2007 to 2008 by 597% due largely to a decrease in net investment income. The decrease in net investment income results from the write-down of certain securities in light of the industry-wide sub-prime mortgage and liquidity crisis experienced in the fall and winter of 2007 and 2008, coupled with fewer invested assets; the amount of invested bond proceeds shrunk as the pre-event auction rate securities were repaid and a significantly smaller amount of debt was issued in 2008. Additionally, the 2008 bond proceeds were invested in tax-exempt, non-AMT investments which provided lower yields.

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.

Citizens Property Insurance Corporation

Management's Discussion & Analysis

Overview of Financial Statements (Continued)

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.

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 17 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.

Citizens Property Insurance Corporation Management's Discussion & Analysis

Financial Analysis

A summary of Citizens' Statements of Net Assets is presented below:

	2008	2007	% Change
	<i>(in thousands)</i>		
Assets			
Current assets	\$ 7,453,317	\$ 8,510,561	(12%)
Capital assets, net	29,253	28,802	2%
Other noncurrent assets	1,234,724	2,804,686	(56%)
Total assets	\$ 8,717,294	\$ 11,344,049	(23%)
Liabilities			
Current liabilities	\$ 3,938,283	\$ 2,691,979	46%
Noncurrent liabilities	1,080,107	5,591,976	(81%)
Total liabilities	5,018,390	8,283,955	(39%)
Net assets			
Invested in capital assets	29,253	28,802	2%
Restricted	24,044	70,585	(66%)
Unrestricted	3,645,607	2,960,707	23%
Total net assets	3,698,904	3,060,094	21%
Total liabilities and net assets	\$ 8,717,294	\$ 11,344,049	(23%)

Assets

As shown above, total assets decreased \$2.6 billion, or 23%, during 2008 primarily due to the decrease in cash and invested assets resulting from the redemption of the \$4.75 billion of outstanding Auction Rate Securities (ARS) during the second quarter of 2008, the permanent markdown of certain distressed investments of \$205.2 million offset by the \$1.75 billion pre-event bond issuance and 2008 net income. Certain investments, representing less than 4% of the portfolio are in defaulted Structured Investment Vehicles. Although principal and interest payments are being made, there is a decline in market value which is being treated as a permanent decline in value for GAAP financial statements. Full realization of the principal value is not readily determinable.

Current assets include cash, cash equivalents, and short-term investments of \$6.8 billion and \$7.7 billion for the years ended 2008 and 2007. Long-term investments totaled \$718 million and \$2.1 billion for the years ended 2008 and 2007. These decreases are due to the \$4.75 billion redemption of the ARS, the market value declines of certain investments, offset by net cash flow from 2008 operations, the collection of emergency assessment funds, the \$1.75 billion HRA

Citizens Property Insurance Corporation Management's Discussion & Analysis

Assets (Continued)

bond issuance and Florida Hurricane Catastrophe Fund ("FHCF") reimbursements received during 2008. During 2007, long-term investments decreased largely to a change in Citizens' investment policy which resulted in a shift in investments from long term assets to short term assets due to a change in the Company's benchmark. The new benchmark was tied to the 30-day LIBOR rate which is shorter in duration than the benchmark previously used.

Capital assets remained consistent with an increase of only 2% from 2007 to 2008.

Liabilities

Total liabilities decreased \$3.3 billion, or 39%, during 2008. This decrease is due primarily to the decrease of \$4.75 billion in long-term debt relating to the redemption of the Auction Rate Securities offset by the issuance of the \$1.75 billion HRA pre-event bond issuance. During 2007, total liabilities increased \$656 million, or 9%. This increase is due primarily to an increase in long-term liabilities resulting from the issuance of \$1.1 billion in tax-exempt post-event refunding bonds and \$950 million in pre-event bonds offset by the maturity and redemption of the 1997 pre-event bonds.

Current liabilities are comprised primarily of loss reserves, loss adjustment expense (LAE) reserves, and unearned premium. Loss and LAE reserves increased \$136 million, or 19%, from 2007 to 2008. The increase in 2008 is attributable to non-hurricane claims. The increase in 2007 is attributable to both hurricane and non-hurricane claims. As of December 31, 2008, reserves related to the 2004 and 2005 hurricanes were \$293 million, as compared to \$290 million as of December 31, 2007, \$212 million as of December 31, 2006 and \$1.2 billion as of December 31, 2005. The increase in hurricane claims reserves in 2007 resulted from adverse development related to new and reopened claims as well as legal proceedings with regard to Citizens liability for storm damage. The decrease in 2006 was due to the payout of claims for the storms of 2004 and 2005.

Unpaid losses and LAE reserves not related to hurricanes increased from \$249 million as of December 31, 2005 to \$376 million as of December 31, 2006 to \$435 million as of December 31, 2007 to \$568 million as of December 31, 2008. The increase in 2008 is due largely to an increase in frequency and severity of sinkhole, fire, theft and water claims. During 2007, the increase was due largely to a continued increase in the Company's overall exposure as it has added more policies to its book of business, which increased dramatically from 2005 to 2006 as a result of approximately 300,000 policies assumed from the insolvent Poe insurance group.

Unearned premiums decreased \$407.5 million, or 25% from 2007 to 2008, which is primarily due to a reduction in premium written, coupled with growth in depopulation during 2008.

Citizens Property Insurance Corporation Management's Discussion & Analysis

Financial Analysis (Continued)

Liabilities (Continued)

During 2007 unearned premiums increased \$19 million, or 1%, primarily due to an increase in direct written premium. The total impact of the increase in direct written premium was largely offset by the depopulation of over 116,000 policies during the last two months of 2007 as insurers began to come back into the state. This had the effect of reducing unearned premium directly.

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

	2008	2007	% Change
	<i>(in thousands)</i>		
Operating revenue:			
Earned premiums	\$ 2,256,628	\$ 3,074,754	(27%)
Operating expenses:			
Losses and LAE incurred	931,636	882,925	6%
Other underwriting expenses	442,570	569,661	(22%)
	1,374,206	1,452,586	(5%)
Operating income	882,422	1,622,168	(46%)
Nonoperating revenues	(244,678)	49,274	(597%)
Gain from operations	637,744	1,671,442	(62%)
Federal income tax benefit	-	2,744	(100%)
Change in net assets	\$ 637,744	\$ 1,674,186	(62%)
Policies in force	1,084,237	1,304,949	(17%)
Underwriting ratios			
Loss and LAE ratio (calendar year)	41%	29%	44%
Expense ratio	20%	19%	6%
Combined ratio	61%	48%	29%

Citizens Property Insurance Corporation

Management's Discussion & Analysis

Financial Analysis (Continued)

Operating Revenue

Direct premium written declined 25% to \$2.77 billion as of December 31, 2008 compared to \$3.72 billion as of December 31, 2007 due to the decline of in force policy count by 17%, combined with the reduction in the average premium. The following factors are related to the decline in average premium: doubling of wind mitigation credits beginning in 2008; increased policyholder take up on wind mitigation credits; the presumed factor for sinkholes and the ability for certain policyholders to reduce their premium by excluding sinkhole coverage. Net earned premiums decreased to \$2.26 billion at December 31, 2008 as compared to \$3.07 billion at December 31, 2007, a decrease of \$818.1 million, or 27%. During 2007, earned premiums increased \$1 billion, or 50%, as compared to 2006. Policy growth leveled out in 2007, however due to the large policy growth that occurred in the latter part of 2006, a significant part of the premium written in 2006 was earned in 2007. This increase is partially offset by refunds issued in early 2007 resulting from legislative changes as well as an increase in premiums ceded to the Florida Hurricane Catastrophe Fund (FHCF) and to companies assuming Citizens' policies.

Policies in force decreased 220,712 policies, or 17% during 2008. This decrease in policy count is a result of increased takeout activity in 2008, coupled with a reduction in new business written. Policies in force stayed fairly level during 2007 with an increase of 6,027 policies, or .05%, during 2007.

During the regular and special legislative sessions of 2007, Citizens' rate increases that were put into effect January 1, 2007, were rescinded. The pre-2007 rates for personal residential policies were deemed to remain in effect through December 31, 2009, except for any rates which were lowered. Therefore, there have been no rate changes during 2008. During 2007, Citizens and other insurers were also required to make rate filings to reflect the savings associated with purchasing additional coverage from the FHCF. As a result of this legislation, Citizens implemented rate decreases and refunds. Citizens' premium rates decreased on average 5.8% and 18.1% for residential policies written in its Personal Lines Accounts (PLA) and High Risk Accounts (HRA), respectively. In addition, the Commercial Lines Accounts (CLA) rates decreased an average of 12.0%.

Premiums ceded to the FHCF totaled \$440.4 million and \$488.3 million during 2008 and 2007, respectively, and are included in net earned premiums. The decrease in FHCF premium is attributed to a decrease in exposure. Ceded premiums to private reinsurers were \$105.1 million in 2008. The Corporation entered into excess of loss reinsurance agreements with private reinsurers in 2008, but not in 2007, for the HRA.

Citizens Property Insurance Corporation

Management's Discussion & Analysis

Financial Analysis (Continued)

Operating Revenue (Continued)

Ceded premiums to takeout companies increased \$100.4 million, or 37%, for 2008. \$369.7 million was ceded to takeout companies during the year ended December 31, 2008 compared to \$269.3 million ceded during the same period in 2007.

Operating Expenses

Losses and LAE incurred increased \$48.7 million, or 6%, in 2008 as compared to 2007, due mainly to an increase in the non-catastrophic claims costs that relate to water, sinkhole and fire claims. The frequency and severity of such claims has increased in 2008, as compared to 2007. Losses and LAE incurred increased \$223 million, or 34%, in 2007 as compared to 2006, due mainly to adverse development in claims related to the 2004 and 2005 hurricanes as well as an increase in the non-catastrophe claims costs.

Other underwriting expenses decreased \$127 million, or 22%, in 2008. Certain underwriting expenses such as agent commissions and premium taxes, are determined based on written premiums and will decrease proportionately. During 2008, commission and premium and other tax expenses consisted of 57% and 12% of other underwriting expenses, respectively. During 2007, other underwriting expenses increased \$248 million, or 77%, and commission and premium and other tax expenses consisted of 52% and 23% of other underwriting expenses, respectively. Additionally, taxes and assessments were unusually high in 2007 as a result of the \$68.0 million assessment by the Florida Insurance Guaranty Association. Administrative and other underwriting expenses include typical administrative costs, professional fees which include servicing carrier fees, and underwriting costs such as inspection fees, and ISO participation fees. Administrative and other expenses increased \$13.6 million, or 13%, in 2008 when compared to the same period in 2007. The increase is primarily related to an increase in full time employees and related expenses thereof and depreciation.

Non-operating Income (Expenses)

Non-operating income/expenses consist mainly of assessment income, net investment income, and interest expense. Non-operating income decreased \$294.0 million, or 597% in 2008 as compared to 2007 which corresponds to the decrease in net investment income of \$330.8 million, or 97%. The decrease in net investment income is due primarily to the decline in overall cash and invested assets. Additionally a permanent markdown on investments of \$205.2 million was recognized in 2008 related to distressed investments purchased on Citizens' behalf by a former money manager. Also, the unrealized losses on certain corporate investments have increased due to widened credit spreads for all corporate issuers, especially financial issuers. In 2007, non-operating income decreased \$1.7 billion, or 97% as compared to 2006 which corresponds to the

Citizens Property Insurance Corporation

Management's Discussion & Analysis

Financial Analysis (Continued)

Non-operating Income (Expenses) (Continued)

decrease in assessment income of \$1.7 billion, or 96%. Assessment income of \$68 million was recognized in 2007 which is related to a FIGA emergency assessment recoupment.

Economic Factors

Citizens' management continues to evaluate the best sources of liquidity as it prepares for the 2009 hurricane season. Subsequent to year end 2007, management determined that its 2004, 2006, and 2007 auction rate securities were not providing the best source of liquidity given the increased interest rates required to be paid as a result of the industry-wide market turmoil of late 2007 and early 2008. Consequently, management determined that the best course of action was to redeem these securities and pursue other sources of liquidity. Management is currently negotiating lines of credit and is considering a new bond issue that would be tied to a fixed rate.

Citizens' High Risk Account bond ratings were upgraded from A3 to A2 by Moody's Investor Service, Inc. ("Moody's") on April 4, 2008. However, both Moody's and Standard and Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P") have recently changed the outlook of Citizens' PLA/CLA and HRA ratings to negative from stable. Such 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 and S&P, 55 Water Street, New York, New York, 10041. 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 2008, management continued to administer programs designed to reduce the number of policies 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. Takeout activity has increased in 2008 as compared to 2007. The private market has responded by removing policies from both the Personal Lines Account and the High-Risk Account. During 2008, 362,964 PLA policies and 21,519 HRA policies were assumed by private insurers, as compared to 247,923 PLA policies and no HRA policies assumed during 2007 and 26,225 PLA policies and 41,628 HRA policies assumed during 2006.

Although not yet implemented, Legislation in 2007 significantly changed the standards Citizens uses to set rates, requiring Citizens to set actuarially sound rates; however, legislation in 2007 and 2008 froze Citizens rates to amounts established in 2006 with no rate increases to be made

Citizens Property Insurance Corporation Management's Discussion & Analysis

Economic Factors (Continued)

until January 1, 2010 at the earliest. There is no assurance that the Florida Legislature will not in 2009 and subsequent years alter, cap or even continue a freeze on Citizens' rates.

Citizens' enabling legislation and Plan of operations established a process by which Citizens may levy 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.

Financial Statements

Citizens Property Insurance Corporation
Statements of Net Assets

	December 31	
	2008	2007
	<i>(In Thousands)</i>	
Assets		
Current assets:		
Cash and cash equivalents	\$ 4,229,514	\$ 3,251,622
Short-term investments	2,584,342	4,453,493
Restricted cash and cash equivalents	24,044	70,585
Deferred policy acquisition costs	112,182	149,921
Investment income due and accrued	9,796	29,400
Prepaid reinsurance premiums	137,154	144,733
Reinsurance recoverable	37,602	122,405
Premiums receivable, net	184,314	126,630
Premiums receivable from assuming companies	24,304	10,989
Current portion of assessment receivables	110,065	150,783
Total current assets	7,453,317	8,510,561
Noncurrent assets:		
Long-term investments	718,004	2,098,685
Deferred takeout bonus	4,865	14,775
Capital assets, net	29,253	28,802
Assessment receivables	509,434	686,243
Other assets	2,421	4,983
Total noncurrent assets	1,263,977	2,833,488
Total assets	\$ 8,717,294	\$ 11,344,049

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Net Assets
(Continued)

	December 31	
	2008	2007
	<i>(In Thousands)</i>	
Liabilities and net assets		
Current liabilities:		
Loss reserves	\$ 698,023	\$ 569,747
Loss adjustment expense reserves	163,442	155,653
Unearned premiums	1,224,342	1,631,878
Reinsurance premiums payable	42,122	42,348
Advance premiums and suspended cash	87,753	130,535
Interest payable	51,627	27,200
Taxes and fees payable	4,651	11,856
Current portion of long-term debt	1,587,641	49,906
Other current liabilities	78,682	72,856
Total current liabilities	3,938,283	2,691,979
Noncurrent liabilities:		
Long-term debt	1,080,107	5,591,976
Total noncurrent liabilities	1,080,107	5,591,976
Total liabilities	5,018,390	8,283,955
Net assets:		
Invested in capital assets	29,253	28,802
Restricted	24,044	70,585
Unrestricted	3,645,607	2,960,707
Total net assets	3,698,904	3,060,094
Total liabilities and net assets	\$ 8,717,294	\$ 11,344,049

See accompanying notes to financial statements.

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

	Years Ended December 31	
	2008	2007
	<i>(In Thousands)</i>	
Operating revenue:		
Premiums earned, net	\$ 2,256,628	\$ 3,074,754
Operating expenses:		
Losses incurred	815,938	711,238
Loss adjustment expenses incurred	115,698	171,687
Service company fees	9,760	13,075
Agent commissions, net	250,858	294,310
Taxes and fees	51,691	130,673
Processing and other fees	2,372	4,469
Other underwriting expenses	118,065	104,504
Takeout bonus expense	9,824	22,630
	1,374,206	1,452,586
Operating income	882,422	1,622,168
Nonoperating revenues (expenses):		
Net investment income	11,740	342,523
Interest expense	(179,624)	(337,630)
Assessment income	-	68,008
Line of credit fees and note issuance costs	(76,794)	(23,627)
Total nonoperating revenues (expenses)	(244,678)	49,274
Gain from operations	637,744	1,671,442
Federal income tax benefit	-	2,744
Change in net assets	637,744	1,674,186
Net assets, beginning of year	3,060,094	1,387,156
Other changes in net assets	1,066	(1,248)
Net assets, end of year	\$ 3,698,904	\$ 3,060,094

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Cash Flows

	Years Ended December 31	
	2008	2007
	<i>(In Thousands)</i>	
Operating activities		
Premiums collected, net of reinsurance	\$ 1,827,693	\$ 3,027,742
Losses and loss adjustment expenses paid	(795,571)	(745,131)
Payments to employees for services	(56,455)	(41,900)
Payments for underwriting expenses	(323,771)	(455,342)
Other operating receipts (payments)	-	170,804
Net cash provided by operating activities	<u>651,896</u>	<u>1,956,173</u>
Noncapital financing activities		
Debt issuance	1,769,880	2,072,577
Debt redemption	(4,800,000)	(1,400,000)
Interest paid	(174,958)	(357,266)
Assessment income received	217,527	202,967
Financing costs paid	(1,048)	(178,906)
Net cash (used in) provided by noncapital financing activities	<u>(2,988,599)</u>	<u>339,372</u>
Capital and related financing activities		
Capital assets acquired	(13,122)	(20,197)
Net cash used in capital and related financing activities	<u>(13,122)</u>	<u>(20,197)</u>
Investing activities		
Proceeds from investments sold, matured or repaid	24,869,920	15,578,511
Investments acquired	(25,187,680)	(15,627,637)
Net investment income paid	3,598,936	(1,777,275)
Net cash used in investing activities	<u>3,281,176</u>	<u>(1,826,401)</u>
Net increase (decrease) in cash and cash equivalents	931,351	448,947
Cash and cash equivalents:		
Beginning of year	3,322,207	2,873,260
End of year	<u>\$ 4,253,558</u>	<u>\$ 3,322,207</u>
Classified as:		
Cash and cash equivalents	\$ 4,229,514	\$ 3,251,622
Restricted cash and cash equivalents	24,044	70,585
	<u>\$ 4,253,558</u>	<u>\$ 3,322,207</u>

See accompanying notes to financial statements.

Citizens Property Insurance Corporation
Statements of Cash Flows
(Continued)

	Years Ended December 31	
	2008	2007
	<i>(In Thousands)</i>	
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 882,422	\$ 1,622,168
Depreciation expense	12,672	8,591
Loss on disposal of capital assets	-	20
Adjustments to reconcile net cash provided by operating activities:		
(Increase) decrease in operating assets:		
Deferred policy acquisition costs	37,739	2,908
Prepaid reinsurance premiums	7,579	(133,395)
Reinsurance recoverable	84,803	6,639
Premiums receivable, net	(70,999)	105,602
Income tax benefit	-	170,804
Deferred takeout bonus	9,910	18,100
Other assets	2,562	(2,078)
Increase (decrease) in operating liabilities:		
Loss and loss adjustment expense reserves	136,065	137,794
Unearned premiums	(407,536)	18,964
Reinsurance premiums payable	(226)	42,341
Advance premiums and suspended cash	(42,782)	(44,822)
Taxes and fees payable	(7,205)	(3,911)
Other current liabilities	5,826	7,696
Other changes in net assets	1,066	(1,248)
Net cash provided by operating activities	<u>\$ 651,896</u>	<u>\$ 1,956,173</u>
Noncash supplementary information		
Net unrealized (gain) loss on investments	<u>\$ 32,219</u>	<u>\$ (4,240)</u>

See accompanying notes to financial statements.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 1 - GENERAL

Citizens Property Insurance Corporation (Citizens) 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 the necessity of Citizens to provide insurance that was affordable.

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 (executive director) 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.

Citizens Property Insurance Corporation

Notes to Financial Statements

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 High-Risk Account. A brief history of each account follows:

Personal Lines Account history - The FRPCJUA 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 (on a statewide basis) 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 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. These policies excluded windstorm coverage on properties within eligible areas. 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.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 1 - GENERAL (CONTINUED)

High-Risk Account history – The FWUA, which was a residual market mechanism for windstorm and hail coverage in selected 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.

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 and interpretations, 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 net assets component as the unspent proceeds. As of December 31, 2008 and 2007, Citizens did not have any outstanding debt that was attributable to capital assets.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (Continued)

- 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.”

Adoption of New Accounting Standards

On January 1, 2006, Citizens adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109. FIN 48 addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements.

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 statement of net assets. The statement of revenues, expenses and changes in net assets presents increases (revenues) and decreases (expenses) in total net assets. The statement of cash flows provides information about how Citizens finances and meets the cash flow needs of its activities.

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. For purposes of the statement of cash flows, highly liquid investments with original maturities of three months or less at the time of acquisition are considered to be cash.

Investments consist of relatively low-risk, highly liquid fixed-income securities. Such investments are recorded at market value, which is 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. Although the estimate reflects an attempt to reasonably reflect stressed circumstances that currently exist, the amount actually realized if the securities were liquidated at any time could be more or less than the estimate. Citizens considers all investments with remaining maturities of one year or less to be short-term.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred Policy Acquisition Costs

Costs which vary directly with acquiring, renewing and servicing an insurance policy such as net agent commissions, servicing company fees and other taxes and fees (see Note 7) are deferred and recognized over the term of the related policy. Amortization of deferred policy acquisition costs recognized for the years ended December 31, 2008 and 2007 was \$319.8 million and \$442.5 million, respectively.

Deferred Takeout Bonus

Takeout bonuses incurred in connection with the depopulation of Citizens (see Note 12) 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.

Capital Assets

Capital assets are stated at cost less related accumulated depreciation. The capitalization threshold for assets purchased in 2008 was increased to \$2,500 from \$1,000. Depreciation is computed using the straight-line method over the estimated useful lives of three to seven years. Depreciation expense for fixed assets was \$12.7 million and \$8.6 million for the years ended December 31, 2008 and 2007.

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, no assurance can be given that the ultimate settlement of losses may not 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 are recorded as earned on a 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

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Premiums (Continued)

allowance for doubtful accounts is recorded for the estimated uncollectible amounts and was \$7.6 million and \$8.2 million at December 31, 2008 and 2007, respectively.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from premiums charged to policyholders. Operating expenses include incurred losses 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

Assessments made pursuant to the Act and the Plan are recognized as revenue and recorded as receivable in the period approved by the Board and verified by the Office for mathematical accuracy (See Note 15). Assessment receivables are considered to be fully collectible.

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 catastrophic reinsurance purchases and depopulation premiums.

Note Issuance Costs

Note issuance costs incurred in connection with acquiring notes payable (see Note 6) are deferred and amortized over the life of the note agreements.

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.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 52.35% of Citizens' insurance coverage exposure lies in the Southeast Florida counties of Miami-Dade, Broward, Monroe and Palm Beach as of December 31, 2008. Approximately 10.83% of Citizens' insurance coverage lies in Pinellas and Hillsborough counties as of December 31, 2008. 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 15).

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, premiums receivable, 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, 2008, management believes the Company had no significant concentrations of credit risk other than those disclosed in Note 3.

Reclassifications

Certain reclassifications have been made to the 2007 amounts to conform to the 2008 presentation.

NOTE 3 - INVESTMENTS

The investment of bond proceeds are required by the bond documents to be held in "permitted investments". Permitted investments generally must be rated in one of the two or three highest rating categories of each of the Rating Agencies, depending on the type of investment. Permitted investments include certificates of deposit, money market funds, U.S. Government or Agency obligations, commercial paper, municipal obligations, corporate securities, guaranteed investment contracts, investments in the Local Government Investment Pool, investments in the Special Purpose Investment Account, and repurchase agreements collateralized by U.S. Government or Agency obligations.

Citizens' short-term investments include shares held in the Local Government Investment Pool ("LGIP") administered by the Florida State Board of Administration. The entire \$58.2 million invested in the LGIP at December 31, 2008 is invested in Fund B, which has been frozen from

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 3 - INVESTMENTS (CONTINUED)

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, 2008 of 0.665824. Fund B is not rated by any nationally recognized statistical rating agency. Citizens recognized a decline in value of \$30.1 million on its holdings in 2008. Full realization of the principal value of Pool B assets is not readily determinable. Citizens withdrew all monies in Fund A by December 31, 2008.

Citizens has adopted both taxable and tax-exempt investment policies which apply to all funds under its control, including bond proceeds. Such investment policy is at least or more restrictive than the bond documents require. 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 fixed or variable rate instruments that have minimum ratings as specified in the investment policy by one of the Rating Agencies. The minimum ratings differ by security type. Any type of investment security or contract that is not specifically identified in the investment policy is prohibited. All securities in the portfolio should have a maximum maturity of 3 years. The entire portfolio must be convertible into cash within 15 business days to provide prompt payment of potential claims.

- **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. All long-term and short-term securities held in the investment portfolio are rated by one of the three Nationally Recognized Rating Agencies. The table which follows is the Market Value by rating classification as reported by Moody's (See discussion of rating agencies in "Economic Factors" under Management's Discussion and Analysis). This table includes debt securities of the US government and obligations of U.S. government agencies that are explicitly guaranteed, including U.S. Treasury and GNMA investments as well as corporate bonds.

Rating	Market Value <i>(in thousands)</i>
A1	\$ 582,154
A2	350,228
A3	322,538
AA1	117,653
AA2	218,131
AA3	61,699
AAA	1,294,361
BAA1	9,632
BAA2	26,065
Not Rated/Rating Withdrawn	316,739
Agency Mortgage Backed Securities	3,146
	\$ 3,302,346

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 3 - INVESTMENTS (CONTINUED)

- **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, 2008 and 2007, 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. Citizens does not have 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 company's investment policy requires that the weighted average maturity of the portfolio not exceed 365 days for those investments managed to the 30 Day LIBOR Index Merrill Lynch L4US. The following table reflects the duration by security type at December 31, 2008:

	Market Value	Weighted Average Maturity
	<i>(in thousands)</i>	
U.S. Government & Agency	\$ 1,256,048	168 Days
Corporate	2,043,152	362 Days
Mortgage Backed Securities	3,146	1,775 Days
	\$ 3,302,346	289 Days

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, 2008 and 2007, respectively. All investments were denominated in U.S. dollars.

NOTE 4 - FIXED ASSETS

A summary of changes in fixed assets and depreciation for the year ended December 31, 2008 follows:

Citizens Property Insurance Corporation
Notes to Financial Statements

NOTE 4 - FIXED ASSETS (CONTINUED)

	Beginning Balance	Additions	Reductions/ Adjustments	Ending Balance
	<i>(in thousands)</i>			
Leasehold improvements	\$ 6,228	\$ 1,130	\$ (100)	\$ 7,258
Furniture and equipment	26,479	6,838	(302)	33,015
Other capital assets	25,753	5,154	-	30,907
Totals at historical cost	<u>58,460</u>	<u>13,122</u>	<u>(402)</u>	<u>71,180</u>
Less accumulated depreciation for:				
Leasehold improvements	(1,241)	(663)	32	(1,872)
Furniture and equipment	(12,587)	(6,262)	274	(18,575)
Other capital assets	(15,830)	(5,650)	-	(21,480)
	<u>(29,658)</u>	<u>(12,575)</u>	<u>306</u>	<u>(41,927)</u>
	<u>\$ 28,802</u>	<u>\$ 547</u>	<u>\$ (96)</u>	<u>\$ 29,253</u>

A summary of changes in fixed assets and depreciation for the year ended December 31, 2007 follows:

	Beginning Balance	Additions	Reductions/ Adjustments	Ending Balance
	<i>(in thousands)</i>			
Leasehold improvements	\$ 3,656	\$ 2,572	\$ -	\$ 6,228
Furniture and equipment	16,316	10,360	(197)	26,479
Other capital assets	18,488	7,265	-	25,753
Totals at historical cost	<u>38,460</u>	<u>20,197</u>	<u>(197)</u>	<u>58,460</u>
Less accumulated depreciation for:				
Leasehold improvements	(768)	(473)	-	(1,241)
Furniture and equipment	(8,777)	(3,976)	166	(12,587)
Other capital assets	(11,699)	(4,142)	11	(15,830)
	<u>(21,244)</u>	<u>(8,591)</u>	<u>177</u>	<u>(29,658)</u>
	<u>\$ 17,216</u>	<u>\$ 11,606</u>	<u>\$ (20)</u>	<u>\$ 28,802</u>

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

Activity in the liability for loss reserves and loss adjustment expense reserves for the years ended December 31, 2008 and 2007 were as follows:

Citizens Property Insurance Corporation
Notes to Financial Statements

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

	2008	2007
	<i>(in thousands)</i>	
Loss reserves and loss adjustment expense reserves, beginning of year	\$ 725,400	\$ 587,606
Incurred related to:		
Current year	839,708	692,583
Prior years	91,928	190,342
Total incurred	931,636	882,925
Paid related to:		
Current year	413,175	353,312
Prior years	382,396	391,819
Total paid	795,571	745,131
Loss reserves and loss adjustment expense reserves, end of year	\$ 861,465	\$ 725,400

As a result of changes in estimates of insured events in prior years, primarily due to the underestimation of costs relating to prior year hurricane claims, the provision for loss and loss adjustment expenses increased by \$91.9 million and \$190.0 million in 2008 and 2007, respectively.

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 tends to rely more heavily on independent adjusting firms for catastrophic events than for non-catastrophic claims. Citizens compensates these firms, depending upon the type or nature of the claims, either on per-day rate or on a graduated fee schedule based on the gross claim amount, consistent with industry standard methods of compensation.

NOTE 6 - BONDS PAYABLE

Series 2004A through 2004I Bonds – During May 2004, Citizens issued \$750 million of senior secured bonds for the purpose of funding losses in the High-Risk account in the event of a future catastrophe. The bonds were issued in multiple series and bear interest at variable, auctioned rates, based on 30-day LIBOR, for generally successive 28-day auction periods. These 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. No principal payments were made during 2007. The bonds were redeemed in May 2008 after the Auction Rate Securities market collapsed.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 6 - BONDS PAYABLE (CONTINUED)

Series 2006A1 through 2006A22 Bonds – During July 2006, Citizens issued \$3.05 billion of senior secured bonds for the purpose of funding losses in the High-Risk account in the event of a future catastrophe. The bonds were issued in multiple series and bear interest at variable, auctioned rates for generally successive 7-day and 28-day auction periods. 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. No principal payments were made during 2007. The bonds were redeemed in May 2008 after the Auction Rate Securities market collapsed.

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, a predecessor of Citizens. 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 twelve 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 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 \$50 million during 2008. No principal payments were made during 2007. Outstanding maturities net of unamortized premiums were \$1.05 billion and \$1.11 billion, respectively, as of December 31, 2008 and 2007.

Series 2007-1 through 2007-10 Bonds – During July 2007, Citizens issued \$950 million of senior secured bonds for the purpose of funding losses in the Personal Lines Account and the Commercial Lines Account in the event of a future catastrophe. The bonds were issued in multiple series and bear interest at variable, auctioned rates for generally successive 7-day auction periods. 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. No principal payments were made during 2007. The bonds were redeemed in April 2008 after the Auction Rate Securities market collapsed.

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 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. No principal

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 6 - BONDS PAYABLE (CONTINUED)

payments were made during 2008. Outstanding maturities net of unamortized premiums were \$1.76 billion as of December 31, 2008.

A schedule of debt service requirements, including principal and interest, is as follows:

Year Ending December 31	Principal	Interest	Total
		<i>(in thousands)</i>	
2009	\$ 1,591,580	\$ 122,531	\$ 1,714,111
2010	96,160	55,887	152,047
2011	350,995	44,803	395,798
2012	106,125	33,422	139,547
2013	111,530	28,019	139,549
2014-2018	506,150	52,041	558,191
Total	\$ 2,762,540	\$ 336,703	\$ 3,099,243

Unamortized net premium at December 31, 2008 was \$52.3 million.

The total interest expense on the Bonds for the years ended December 31, 2008 and 2007 was \$162.9 million and \$310.8 million including amortized premium of \$19.8 million and amortized premium of \$3.5 million, respectively, and is included in interest expense in the accompanying statements of revenues, expenses and changes in net assets.

Total deferred issuance costs related to all notes was \$147.0 million and \$222.8 million at December 31, 2008 and 2007 and is included in "Long term debt" in the Statement of Net Assets. Total bond premium related to all notes was \$52.3 million and \$52.1 million at December 31, 2008 and 2007 and is also included in "Long term debt" in the Statement of Net Assets.

A summary of changes in long-term liabilities for the year ended December 31, 2008 follows (in thousands):

Citizens Property Insurance Corporation
Notes to Financial Statements

NOTE 6 - BONDS PAYABLE (CONTINUED)

	12/31/2007	Additions	Reductions	12/31/2008	Due within one year
Bonds Payable - Face	\$ 5,812,540	\$ 1,750,000	\$(4,800,000)	\$ 2,762,540	\$ 1,591,580
Less Deferred Issuance Costs and Bond Discount/Premium	(170,658)	13,014	62,852	(94,792)	(3,939)
Bonds Payable	\$ 5,641,882	\$ 1,763,014	\$ (4,737,148)	\$ 2,667,748	\$ 1,587,641

Interest Rate Swap Agreements – Citizens had no interest rate exchange agreements outstanding at December 31, 2008 and 2007. However, in connection with the issuance of the Series 1997A Notes issued May 13, 1997, Citizens entered into interest rate exchange agreements with various counterparties for notional amounts of \$500 million. The interest rate exchange agreements were terminated during 1998, 2001 and 2002, for which Citizens received termination payments of \$7.3 million, \$7.6 million, and \$10.3 million, respectively. The gain on the terminated interest rate swap agreements was deferred and amortized over the remaining term of the terminated agreements using the effective interest method. The total amount of deferred gain and accrued interest amortized and recognized as a reduction of interest expense for the years ended December 31, 2008 and 2007 was \$0 and \$1.0 million, respectively. The remaining term of the terminated agreements expired in May 2007.

NOTE 7 - 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.

Additionally, Citizens has entered into agreements with two servicing companies to provide certain services. The first servicing company provides underwriting and policy management services. The agreements related to these services provide for monthly compensation to the companies based on a “Per Transaction Fee” applied to the number of transactions processed in a monthly cycle. The second servicing company provides underwriting, policy management, premium collection, claims administration and claims payment services; claim services were eliminated from this agreement beginning February 19, 2008 and this agreement expired on November 15, 2008 (with policy servicing in a run-off stage through the end of the policy periods). These agreements provide for monthly compensation to the company based on a

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 7 - AGENT COMMISSIONS AND SERVICING COMPANY FEES (CONTINUED)

portion decreasing from 15% to 6% of the related policies' net written premium as total net written premium increases. In addition, the agreement provides for the servicing company to receive policy issuance fees, as well as inspection fees. Service company fees included in the statements of revenues, expenses and changes in net assets were \$9.8 million and \$13.1 million, during 2008 and 2007, respectively.

NOTE 8 - 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.

During 2002, the FWUA transferred its assets and liabilities to Citizens in accordance with Florida Statute 627.351(6). At that time, Citizens filed a federal income tax refund claim in excess of \$182.0 million related to the transfer. Citizens initially received a refund of approximately \$54.9 million from the Internal Revenue Service (the IRS). However, the Internal Revenue Service filed a counterclaim against Citizens seeking payment of past due taxes and interest in the amount of approximately \$93.0 million. Given the uncertainty surrounding its tax position, Citizens recorded the \$54.9 million refund as a liability. In 2005, Citizens on behalf of the FWUA, filed suit against the IRS asserting that for tax years 1999-2002, the FWUA was a non-taxable entity. In September 2006, Citizens and the IRS mediated a settlement of the suit. Under the settlement, the IRS would relinquish any claim against the FWUA for back taxes and also agreed to pay the FWUA a refund of approximately \$120.0 million of previous taxes paid plus accrued interest. Citizens adopted the provisions of FASB Interpretation No. 48, Accounting for Income Taxes, on January 1, 2006. As a result of the implementation of Interpretation 48, Citizens recorded a tax benefit of \$220.5 million which included interest of \$45.0 million. In addition, a gain of \$28.0 million was recognized in 2006 for the expected refund of state income taxes resulting from the federal settlement, which was ultimately collected in full during 2007. In 2007, Citizens recorded a tax benefit of \$2.7 million, which was interest earned in 2007 on the income tax recoverable which was received in April 2007 and is included in income tax benefit (expense) in the accompanying financial statements.

NOTE 9 - LINE OF CREDIT AGREEMENTS

Effective May 15, 2008, Citizens entered into a \$1.67 billion credit agreement (the 2008 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 2008 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. The expiration of the

Citizens Property Insurance Corporation Notes to Financial Statements

NOTE 9 - LINE OF CREDIT AGREEMENTS (CONTINUED)

agreement is May 14, 2009. Citizens is required to pay an annual Facility Fee of .70% on the unused portion of the facility. This rate is based on Moody's and S&P ratings 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 (See discussion of rating agencies in "Economic Factors" under Management's Discussion and Analysis). Unused facility fee expense and closing fees associated with this credit agreement were \$4.68 million and \$1.85 million for the year ended December 31, 2008, respectively. As of December 31, 2008, there were no amounts outstanding under this agreement.

Effective July 3, 2007, Citizens entered into a \$1.0 billion credit agreement (the 2007 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 2007 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. The expiration of the agreement was July 1, 2008. Citizens is required to pay an annual Facility Fee of .20% on the unused portion of the facility. This rate is based on Moody's and S&P ratings 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 (See discussion of rating agencies in "Economic Factors" under Management's Discussion and Analysis). Unused facility fee expenses associated with this credit agreement were \$.8 million and \$1.0 million for the years ended December 31, 2008 and 2007, respectively. Closing fees paid for this credit agreement were \$.5 million for the year ended December 31, 2007.

NOTE 10 - REINSURANCE AGREEMENTS

Citizens participates in the Florida Hurricane Catastrophe Fund (the FHCF). The FHCF will reimburse Citizens a specified percentage of losses incurred relating to a hurricane in Florida if a prescribed retention is reached. Premiums ceded to the FHCF, net of refunds received, totaled \$440.4 million and \$488.3 million, respectively, during 2008 and 2007 and are included in "Premiums earned" in the accompanying statements of revenues, expenses, and changes in net assets. The High-Risk 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.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 10 - REINSURANCE AGREEMENTS (CONTINUED)

	2008		2007	
	Coverage Amounts	Retention Amounts	Coverage Amounts	Retention Amounts
Personal and Commercial Lines				
Accounts	\$ 2,015 million	\$ 779 million	\$ 2,628 million	\$ 983 million
High-Risk Account	3,871 million	1,497 million	4,212 million	1,576 million

Citizens purchased private reinsurance for the High Risk Account in 2008. 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 \$105.1 million during 2008 and are included in "Net written premiums" in the accompanying statements of revenues, expenses, and changes in net assets. Citizens did not purchase private reinsurance in 2007. The private reinsurance coverages and retention amounts by account were as follows:

	2008	
	Coverage Amounts	Retention Amounts
High-Risk Account	\$ 446 million	\$ 1,671 million

The effect of reinsurance on premiums written and earned is as follows:

	2008		2007	
	Premiums		Premiums	
	Written	Earned	Written	Earned
	<i>(in thousands)</i>			
Direct	\$ 2,771,846	\$ 3,179,382	\$ 3,717,971	\$ 3,699,006
Ceded	(915,176)	(922,754)	(757,646)	(624,252)
Net premiums	\$ 1,856,670	\$ 2,256,628	\$ 2,960,325	\$ 3,074,754

Citizens is entitled to \$1.1 billion in FHCF reimbursements and to \$49.3 million in private reinsurance reimbursements in the High Risk Account related to losses incurred and paid as a result of hurricane Wilma in 2005. Citizens is also entitled to \$93.5 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. The losses incurred and the loss adjustment expenses incurred are presented net of these anticipated recoveries in the accompanying statements of revenues, expenses, and changes in net assets. FHCF recoveries of \$868.0 million and private reinsurance recoveries of \$116.1 million were received as of December 31, 2008.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 10 - REINSURANCE AGREEMENTS (CONTINUED)

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 the Company's 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.

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

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 \$2.5 million and \$2.0 million for the years ended December 31, 2008 and 2007, 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").

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 12 - DEPOPULATION (CONTINUED)

During 2008 and 2007, Citizens ceded \$369.7 million and \$269.3 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. 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, 2008 and 2007, assumed premiums in the amount of \$22.8 million and \$7.0 million were due from certain Takeout Companies.

Certain agreements provide for a policy takeout bonus of up to 25% of 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 2008 and 2007, Citizens paid \$8.3 million and \$15.6 million, respectively, out of escrow (net of certain recoveries). During 2008 and 2007, Citizens paid \$1.0 million and \$6.5 million into escrow in accordance with the policy takeout agreements for policies removed in 2007. Citizens did not have a takeout bonus policy in effect for 2008 depopulation programs. The 2008 funding of escrow was an adjustment for bonus policies removed in 2007. 385,084 policies were removed from Citizens in 2008 pursuant 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. 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 2008 and 2007, Citizens paid into escrow \$0 for underfunded accounts and received \$1.1 million and \$1.9 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 \$6.0 million for the years ended December 31, 2008 and 2007.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 13 - OPERATING LEASES (CONTINUED)

At December 31, 2008, future minimum payments under operating leases are as follows (in thousands):

2009	\$ 4,465
2010	4,187
2011	3,394
2012	2,088
2013	2,141
2014 to 2015	1,901
Total	<u>\$ 18,176</u>

NOTE 14 - COMMITMENTS AND CONTINGENCIES

Citizens has been informed that the Securities and Exchange Commission, the Florida Office of Financial Regulation, 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.

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 therefrom, 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 this litigation, Citizens has not determined the affect, if any, on the financial condition or results of operations.

A summary of potentially significant litigation follows:

Poe & Associates, L.L.C. (“Associates”) v. Citizens. 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. (See Note 16). Associates seeks significant damages. Its many claims include breach of contract, tortious interference, equal protection violations, and regulatory taking. Citizens believes it will ultimately prevail on all claims presented.

Overhead and Profit. Two related putative class actions seek damages based on Citizens' alleged failure to pay general contractors’ overhead and profit (“O&P”) under actual cash value (“ACV”) provisions of Citizens’ policies. Limited class discovery is underway. A similar putative class claim has been filed in a pending motion to amend a complaint in an unrelated case. Citizens believes that these cases are not suitable for class action treatment. Citizens has not determined the potential financial exposure, if any, of these lawsuits.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 14 - COMMITMENTS AND CONTINGENCIES (CONTINUED)

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 2008, Citizens had insurance 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 - 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 accounting principles generally accepted in the United States adjusted for certain items.

In the event of a Plan Year Deficit in an 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

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 15 - ASSESSMENTS (CONTINUED)

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 was only the 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. 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 16 - POE FINANCIAL GROUP POLICYHOLDERS

In 2006, the Florida Legislature amended Citizens' enabling statute to provide that, if ordered by a court of competent jurisdiction, Citizens could "assume policies or otherwise provide coverage for policyholders of an insurer placed in liquidation under chapter 631 under such forms, rates, terms, and conditions as the corporation deems appropriate, subject to approval by the Office and ordered by the liquidation court.

Three insurers affiliated with Poe Financial Group, Inc. - Southern Family Insurance Company, Atlantic Preferred Insurance Company, and Florida Preferred Property Insurance Company (the "Poe Insurers") - were placed into liquidation by court order. The Florida Department of Financial Services, Division of Rehabilitation and Liquidation, was named the Receiver of the Poe Insurers. Under the court order and Florida law, coverage with the Poe Insurers ended on July 1, 2006.

A liquidation plan was approved by the Office of Insurance Regulation (OIR) and ordered by the court whereby, effective July 1, 2006, Citizens was to provide transition insurance coverage ("Transition Policies") to eligible policyholders of the Poe Insurers who could not obtain private coverage. Policy claims on losses occurring during the transition period (i.e. from July 1, 2006 until the expiration of the original Poe Insurer policy period), were processed and paid by Citizens. Any losses incurred on policies of the Poe Insurers prior to July 1, 2006 were processed and paid by FIGA.

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 16 - POE FINANCIAL GROUP POLICYHOLDERS (CONTINUED)

Under a 2006 amendment to the statute governing the Florida Hurricane Catastrophe Fund (FHCF), Citizens was able to purchase FHCF coverage for the Transition Policies at a cost of about \$75.0 million for \$1.0 billion of coverage.

Citizens received approximately 308,000 homeowner and 1,700 commercial residential policies as a result of the Transition Policies. To assist with the increased business to Citizens, Citizens hired an additional 160 employees who were formerly employees of affiliates of the Poe Insurers in Tampa.

As the Transition Policies expired, policyholders were required to reapply to Citizens for coverage under Citizens policy forms and eligibility requirements. All transition policies had expired by June 30, 2007.

The Unearned Premium Due to Citizens for providing the transition coverage was calculated by the Receiver, i.e. the Department of Financial Services, and will be paid by FIGA. Under the Plan of Liquidation, FIGA must pay the unearned premium due to Citizens in six installments over three years. Citizens has received payments of \$158.6 million from FIGA through December 2008.

Citizens recorded an estimate of the unearned premium as of July 1, 2006 and recognized an estimate of the earned premium each month thereafter. Additionally, Citizens has recorded an amount receivable due from FIGA. As of December 31, 2007, the receivable due from FIGA was \$74.3 million. As of December 31, 2008, the receivable due from FIGA was \$61.7 million and is included in Premiums receivable, net in the accompanying financial statements. This receivable is net of a guaranty fund assessment FIGA levied on Citizens in October 2007 of \$68.0 million. Citizens has also recorded a receivable for the recoupment of this assessment from its policyholders. Citizens has twelve months to recoup the assessment beginning from the time Citizens first begins to bill its policyholders.

NOTE 17 - SUBSEQUENT EVENTS

2009 HRA Senior Secured Bonds

At the March 10, 2009 Citizens Board of Governors meeting, the Board approved the Bond Resolution authorizing the proposed issuance of up to \$2.5 billion of HRA Series 2009 bonds. The HRA 2009 Bonds will be issued as part of a previously approved liquidity financing program in preparation for the 2009 hurricane season to provide liquidity for the payment of claims should a catastrophic event occur. This financing is to provide a liquidity bridge to pay claims until Citizens is reimbursed by the Florida Hurricane Catastrophe Fund. HRA Series 2009 is expected to be issued in the following structure:

Citizens Property Insurance Corporation

Notes to Financial Statements

NOTE 17 - SUBSEQUENT EVENTS (CONTINUED)

2009 HRA Senior Secured Bonds (Continued)

- Fixed rate, tax-exempt bonds with maturities ranging from 1 to 5 years;
- Issuance may be in more than one series, with some separation between issuances to allow for market absorption;
- First issuance taking place in April, 2009, after the expiration of the appeal period for the required OIR order approving the financing;
- Subsequent issuances (if needed) taking place as soon as practicable thereafter but preferably prior to the start of hurricane season on June 1st; and
- The Bond Resolution and OIR Order are structured to allow for multiple issuances as part of the 2009 financing plan.

There is no assurance that Citizens will close this financing in whole or in part as planned.

2009 PLA/CLA Line of Credit (2009 LOC)

At its April 3, 2009 meeting, Citizens' Board of Governors approved a \$400 million 364-day revolving bank line of credit. Although commitments from lenders are over-subscribed, there is no assurance that Citizens will close the credit agreement in whole or in part as planned. The 2009 PLA/CLA LOC is being entered into as part of a previously approved liquidity financing program in preparation for the 2009 hurricane season, which will provide liquidity for Citizens PLA/CLA in the payment of claims should a catastrophic event occur. This funding is a liquidity bridge to pay claims until Citizens is reimbursed by the Florida Hurricane Catastrophe Fund. The 2009 LOC will replace the existing \$1.665 billion 2008 PLA/CLA LOC, which was put in place for the 2008 hurricane season. Citizens external liquidity needs have reduced significantly because of the growth in PLA/CLA surplus and decline in the number of policies and exposure as a result of continued depopulation activity.

NOTE 18 - RESTRICTED CASH

This restriction of cash 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 Florida Office of Insurance Regulation, 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.

Supplementary Information

Citizens Property Insurance Corporation
Supplemental Combining Statement of Net Assets

December 31, 2008

	Combined	Personal Lines Account	Commercial Lines Account	High Risk Account
<i>(In Thousands)</i>				
Assets				
Current assets:				
Cash and cash equivalents	\$ 4,229,514	\$ 1,161,507	\$ 356,111	\$ 2,711,896
Short-term investments	2,584,342	1,021,231	501,932	1,061,179
Restricted cash and cash equivalents	24,044	-	-	24,044
Deferred policy acquisition costs	112,182	35,391	19,414	57,377
Investment income due & accrued	9,796	4,273	132	5,391
Prepaid reinsurance premiums	137,154	124,787	1,372	10,995
Reinsurance recoverable	37,602	11,389	8,018	18,195
Premiums receivable, net	184,314	115,972	8,213	60,129
Premiums receivable from assuming companies	24,304	22,015	608	1,681
Current portion of assessment receivables	110,065	25,548	8,155	76,362
Total current assets	<u>7,453,317</u>	<u>2,522,113</u>	<u>903,955</u>	<u>4,027,249</u>
Noncurrent assets:				
Long-term investments	718,004	451,959	(114,192)	380,237
Deferred takeout bonus	4,865	4,865	-	-
Capital assets, net	29,253	29,253	-	-
Assessment receivables	509,434	-	-	509,434
Other assets	2,421	1,499	90	832
Inter-account receivable (payable)	-	(433,828)	370,402	63,426
Total noncurrent assets	<u>1,263,977</u>	<u>53,748</u>	<u>256,300</u>	<u>953,929</u>
Total assets	<u>\$ 8,717,294</u>	<u>\$ 2,575,861</u>	<u>\$ 1,160,255</u>	<u>\$ 4,981,178</u>
Liabilities and net assets				
Current liabilities:				
Loss reserves	\$ 698,023	\$ 356,802	\$ 121,602	\$ 219,619
Loss adjustment expense reserves	163,442	108,191	20,231	35,020
Unearned premiums	1,224,342	557,448	142,234	524,660
Reinsurance premiums payable	42,122	833	-	41,289
Advance premiums and suspended cash	87,753	36,765	12,890	38,098
Interest payable	51,627	-	-	51,627
Taxes and fees payable	4,651	3,559	645	447
Current portion of long-term debt	1,587,641	-	-	1,587,641
Other current liabilities	78,682	63,129	2,764	12,789
Total current liabilities	<u>3,938,283</u>	<u>1,126,727</u>	<u>300,366</u>	<u>2,511,190</u>
Noncurrent liabilities:				
Long-term debt	1,080,107	-	-	1,080,107
Total liabilities	<u>5,018,390</u>	<u>1,126,727</u>	<u>300,366</u>	<u>3,591,297</u>
Net assets:				
Invested in capital assets	29,253	29,253	-	-
Restricted	24,044	-	-	24,044
Unrestricted	3,645,607	1,419,881	859,889	1,365,837
Total net assets	<u>3,698,904</u>	<u>1,449,134</u>	<u>859,889</u>	<u>1,389,881</u>
Total liabilities and net assets	<u>\$ 8,717,294</u>	<u>\$ 2,575,861</u>	<u>\$ 1,160,255</u>	<u>\$ 4,981,178</u>

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

Year Ended December 31, 2008

	Combined	Personal Lines Account	Commercial Lines Account	High Risk Account
	<i>(In Thousands)</i>			
Operating revenue:				
Premiums earned	\$ 2,256,628	\$ 1,055,669	\$ 376,277	\$ 824,682
Operating expenses:				
Losses incurred	815,938	576,356	80,448	159,134
Loss adjustment expenses incurred	115,698	77,891	13,964	23,843
Service company fees	9,760	8,716	1,044	-
Agent commissions, net	250,858	84,922	49,331	116,605
Taxes and fees	51,691	26,172	7,350	18,169
Processing and other fees	2,372	1,204	1,168	-
Other underwriting expenses	118,065	58,684	14,728	44,653
Takeout bonus expense	9,824	5,076	-	4,748
Total operating expenses	<u>1,374,206</u>	<u>839,021</u>	<u>168,033</u>	<u>367,152</u>
Operating income	882,422	216,648	208,244	457,530
Nonoperating revenues (expenses):				
Net investment income	11,740	(3,939)	28,955	(13,276)
Interest expense	(179,624)	(12,295)	(3,785)	(163,544)
Line of credit fees and note issuance costs	(76,794)	(14,364)	(4,444)	(57,986)
Total nonoperating revenues	<u>(244,678)</u>	<u>(30,598)</u>	<u>20,726</u>	<u>(234,806)</u>
Gain from operations	637,744	186,050	228,970	222,724
Change in net assets	<u>637,744</u>	<u>186,050</u>	<u>228,970</u>	<u>222,724</u>
Net assets, beginning of year	3,060,094	1,263,084	630,920	1,166,090
Other changes in net assets	1,066	-	-	1,066
Net assets, end of year	<u>\$ 3,698,904</u>	<u>\$ 1,449,134</u>	<u>\$ 859,890</u>	<u>\$ 1,389,880</u>

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

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Net earned premiums and investment revenue	\$ 480,933	\$ 462,207	\$ 575,853	\$ 754,581	\$ 929,691	\$ 1,129,092	\$ 1,143,973	\$ 2,289,760	\$ 3,417,277	\$ 2,268,368
Unallocated expenses	267,415	258,843	254,407	283,265	150,578	191,333	227,795	321,522	569,661	442,570
Estimated incurred claims and expense, end of policy year	112,544	35,855	64,812	97,373	243,767	2,721,512	2,138,004	339,770	692,583	839,708
Paid (cumulative) as of:										
End of policy year	69,471	19,544	41,602	44,863	123,943	1,145,602	1,005,020	157,640	353,312	413,175
One year later	104,241	27,795	59,874	77,758	200,635	2,952,024	2,114,174	291,045	555,540	
Two years later	111,348	28,941	63,625	82,694	215,997	3,234,575	2,227,283	326,997		
Three years later	113,198	29,830	64,809	85,512	222,743	3,377,401	2,286,765			
Four years later	112,419	30,089	68,315	86,402	224,527	3,459,449				
Five years later	112,798	31,186	68,439	86,738	225,999					
Six years later	120,661	30,924	68,547	87,041						
Seven years later	121,034	31,032	68,629							
Eight years later	121,331	31,116								
Nine years later	122,039									
Reestimated incurred claims and expense:										
End of policy year	112,544	35,855	64,812	97,373	243,767	2,721,512	2,138,004	339,770	692,583	839,708
One year later	116,215	31,832	67,838	87,937	222,519	3,285,721	2,205,877	354,194	678,130	
Two years later	118,408	31,698	66,654	87,011	227,916	3,539,287	2,374,726	359,950		
Three years later	119,342	30,932	66,564	88,085	227,956	3,546,902	2,406,456			
Four years later	117,406	30,652	69,337	87,365	227,454	3,615,254				
Five years later	114,217	31,648	69,269	87,188	228,178					
Six years later	121,705	31,487	68,770	87,200						
Seven years later	121,435	31,075	68,684							
Eight years later	121,652	31,134								
Nine years later	122,524									
Increase (decrease) in estimated incurred claims and expense from end of policy year	872	59	(86)	12	724	68,352	31,730	5,756	(14,453)	-

Other Reports

**Independent Auditors' Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of the Financial
Statements in Accordance With *Government Auditing Standards***

The Board of Governors and Management
Citizens Property Insurance Corporation
Tallahassee, FL

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 years ended December 31, 2008 and 2007, and have issued our report thereon dated April 15, 2009. We conducted our audits in accordance with auditing standards generally accepted in the United States 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

In planning and performing our audits, we considered Citizens' 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' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Citizens' internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects Citizens' ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of Citizens' financial statements that is more than inconsequential will not be prevented or detected by Citizens' internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by Citizens' internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material

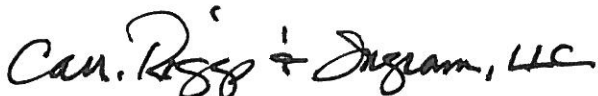
weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Citizens' 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 that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of Citizens in a separate letter dated April 15, 2009.

This report is intended solely for the information and use of the Board of Governors, management and the 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.


Carr, Riggs & Ingram, LLC
April 15, 2009