

Texas Windstorm Insurance Association

Statutory Financial Statements and Supplemental Information

Years Ended December 31, 2019 and 2018



**Texas Windstorm Insurance
Association**

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Texas Windstorm Insurance Association

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Accountants' Letter of Qualifications

Board of Directors
Texas Windstorm Insurance Association

We have audited, in accordance with auditing standards generally accepted in the United States of America, the statutory financial statements of Texas Windstorm Insurance Association (the "Association") for the years ended December 31, 2019 and 2018, and have issued our report thereon dated April 23, 2020. In connection therewith, we advise you as follows:

- a. We are independent certified public accountants with respect to the Association and conform to the standards of the accounting profession as contained in the Code of Professional Conduct and pronouncements of the American Institute of Certified Public Accountants, and the Rules of Professional Conduct of the Texas State Board of Public Accountancy.
- b. The engagement partner, who is a certified public accountant, has 26 years of experience in public accounting and is experienced in auditing insurance enterprises. Members of the engagement team, most of whom have had experience in auditing insurance enterprises and most of whom are certified public accountants, were assigned to perform tasks commensurate with their training and experience.
- c. We understand that the Association intends to file its audited statutory financial statements and our report thereon with the Texas Department of Insurance and that the Insurance Commissioner of that state will be relying on that information in monitoring and regulating the statutory financial condition of the Association.

While we understand that an objective of issuing a report on the statutory financial statements is to satisfy regulatory requirements, our audit was not planned to satisfy all objectives or responsibilities of insurance regulators. In this context, the Association and Insurance Commissioner should understand that the objective of an audit of statutory financial statements in accordance with auditing standards generally accepted in the United States of America is to form an opinion and issue a report on whether the statutory financial statements present fairly, in all material respects, the admitted assets, liabilities, surplus and other funds, results of operations and cash flows in conformity with accounting practices prescribed or permitted by the Texas Department of Insurance. Consequently, under auditing standards generally accepted in the United States of America, we have the responsibility, within the inherent limitations of the auditing process, to plan and perform our audit to obtain reasonable assurance about whether the statutory financial statements are free of material misstatement, whether caused by error or fraud, and to exercise due professional care in the conduct of the audit. The concept of selective testing of the data being audited, which involves judgment both as to the number of transactions to be audited and the areas to be tested, has been generally accepted as a valid and sufficient basis for an auditor to express an opinion on financial statements. Audit procedures that are effective for detecting errors, if they exist, may be ineffective for detecting misstatements resulting from fraud. Because of the characteristics of fraud, particularly those involving concealment and falsified documentation (including forgery), a properly planned and performed audit may not detect a material misstatement resulting from fraud. In addition, an audit does not address the possibility

that material misstatements resulting from fraud may occur in the future. Also, our use of professional judgment and the assessment of materiality for the purpose of our audit means that matters may exist that would have been assessed differently by the Insurance Commissioner.

It is the responsibility of the management of the Association to adopt sound accounting policies, to maintain an adequate and effective system of accounts, and to establish and maintain an internal control structure that will, among other things, provide reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in conformity with accounting practices prescribed or permitted by the Texas Department of Insurance.

The Insurance Commissioner should exercise due diligence to obtain whatever other information that may be necessary for the purpose of monitoring and regulating the statutory financial position of insurers and should not rely solely upon the independent auditor's report.

- d. We will retain the workpapers prepared in the conduct of our audit until the Texas Department of Insurance has filed a Report of Examination covering 2019, but not longer than seven years. After notification to the Association, we will make the workpapers available for review by the Texas Department of Insurance at the offices of the insurer, at our offices, at the Insurance Department or at any other reasonable place designated by the Insurance Commissioner. Furthermore, in the conduct of the aforementioned periodic review by the Texas Department of Insurance, photocopies of pertinent audit working papers may be made (under the control of the accountant) and such copies may be retained by the Texas Department of Insurance.
- e. The engagement partner has served in that capacity with respect to the Association since 2018, is licensed by the Texas State Board of Public Accountancy, and is a member in good standing of the American Institute of Certified Public Accountants.
- f. To the best of our knowledge and belief, we are in compliance with the requirements of section 7 of the NAIC's Model Rule (Regulation) Requiring Annual Audited Financial Reports regarding qualifications of independent certified public accountants.

This letter is intended solely for the information and use of the Texas Department of Insurance and is not intended to be and should not be used by anyone other than these specified parties.

Carl Thomas & Metzger, LLP

April 23, 2020

Independent Auditors' Report

Board of Directors
Texas Windstorm Insurance Association
Austin, Texas

We have audited the accompanying statutory statements of admitted assets, liabilities, surplus and other funds of Texas Windstorm Insurance Association (the "Association") as of December 31, 2019 and 2018 and the related statutory statements of income and changes in surplus and other funds, and cash flows for the years then ended, and the related notes to the statutory financial statements.

Management's Responsibility for the Statutory Financial Statements

Management is responsible for the preparation and fair presentation of these statutory financial statements in accordance with accounting practices prescribed or permitted by the Texas Department of Insurance; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the statutory financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these statutory financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statutory financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the statutory financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the statutory financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the statutory financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the statutory financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis of Accounting

As described more fully in the Summary of Significant Accounting Policies, these financial statements were prepared in conformity with accounting practices prescribed or permitted by the Texas Department of

Insurance, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

Because of the differences between statutory accounting principles and accounting principles generally accepted in the United States of America identified above, as of December 31, 2019 and 2018 total assets were lower by approximately \$8.3 million and \$8.9 million, respectively. The differences identified above reduced total net position as of December 31, 2019 and 2018 by approximately \$11.3 million and \$10.1 million, respectively. The effects on change in net position for the years ended December 31, 2019 and 2018 were immaterial.

Adverse Opinion on Accounting Principles Generally Accepted in the United States of America

In our opinion, because of the effects of the matters discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Texas Windstorm Insurance Association as of December 31, 2019 and 2018, or the results of its operations or its cash flows for the years then ended.

Opinion on Statutory Basis of Accounting

In our opinion, the statutory financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, surplus and other funds of the Texas Windstorm Insurance Association as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in the Summary of Significant Accounting Policies – “Basis of Accounting”.

Emphasis of Matters

As of December 31, 2019, the Association had approximately \$61 billion of insurance exposure in certain designated counties located in the gulf coast region of the State of Texas. By state statute, the Association is prohibited from maintaining a surplus by virtue of its funding obligations to the Catastrophe Reserve Trust Fund (“CRTF”); any net gain from operations must be paid to the CRTF. As of December 31, 2019, the balance in the CRTF was approximately \$122.5 million. If a major claim event occurs in the future, it could have a severe impact on the financial condition of the Association.

In accordance with Senate Bill 900 (“SB 900”) passed by the Texas Legislature during 2015, the Association is authorized to place \$1.0 billion in public securities and assess member insurance companies \$1.0 billion to fund catastrophic losses. The Association does not have taxing authority. In addition, the public securities, if issued, will not be guaranteed by any state or federal agency. Consequently, the ability of the Association to place all these public securities and the sufficiency of that amount to cover future losses will depend upon market conditions and the financial and operating results of the Association.

Ultimate loss projections for Hurricane Harvey were estimated to be \$1.7 billion by the Association’s appointed actuary as of December 31, 2019. If the ultimate loss projection changes in the future it could have a material adverse effect on the financial condition of the Association.

Supplemental Information

Our audits of the statutory financial statements were conducted for the purpose of forming an opinion on those statements as a whole. The accompanying supplementary information is presented to comply with the National Association of Insurance Commissioners' Accounting Practices and Procedures Manual and Texas state law. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the statutory financial statements. The information has been subjected to the auditing procedures applied in the audit of the statutory financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the statutory financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the statutory financial statements as a whole.

Cahn, Therman & Matza, LLP

April 23, 2020

Texas Windstorm Insurance Association

Statutory Statements of Admitted Assets, Liabilities, Surplus and Other Funds (Amounts in Thousands)

<i>December 31,</i>	2019	2018
Admitted Assets		
Cash and cash equivalents	\$ 514,611	\$ 656,127
Assessment receivable	90,000	-
Other assets	1,506	1,712
Total admitted assets	\$ 606,117	\$ 657,839
Liabilities, Surplus and Other Funds		
Liabilities:		
Loss and loss adjustment expenses	\$ 169,130	\$ 200,780
Borrowed money – bonds and interest payable	331,742	383,701
Underwriting expenses payable	9,962	9,822
Unearned premiums	185,495	195,050
Ceded reinsurance premiums payable, net of ceding commissions	22,381	20,172
Funds held by company under reinsurance treaties	179	400
Statutory fund payable	52,641	110,590
Other liabilities	18,379	15,188
Total liabilities	789,909	935,703
Commitments and contingencies (Notes 7, 8, 9, 12, 14 and 15)		
Surplus and other funds:		
Unassigned deficit	(183,792)	(277,864)
Total liabilities and surplus and other funds	\$ 606,117	\$ 657,839

See accompanying summary of significant accounting policies and notes to statutory financial statements.

Texas Windstorm Insurance Association

Statutory Statements of Income (Amounts in Thousands)

<i>Years ended December 31,</i>	2019	2018
Underwriting income:		
Premiums earned	\$ 381,571	\$ 409,954
Premiums ceded	(94,094)	(108,439)
Net premiums earned	287,477	301,515
Deductions:		
Losses and loss expenses incurred	113,398	175,998
Underwriting expenses incurred	92,415	96,399
Total underwriting deductions	205,813	272,397
Net underwriting gain	81,664	29,118
Investment loss:		
Net investment loss	(22,117)	(27,331)
Other income:		
Assessment income	90,000	281,820
Other income	43	52
Total other income	90,043	281,872
Net income before statutory fund cost and federal income tax expense	149,590	283,659
Statutory fund cost	52,641	110,590
Net income before federal income tax expense	96,949	173,069
Federal income taxes incurred	-	-
Net income	\$ 96,949	\$ 173,069

See accompanying summary of significant accounting policies and notes to statutory financial statements.

Texas Windstorm Insurance Association

Statutory Statements of Changes In Surplus and Other Funds (Amounts in Thousands)

		Unassigned Deficit
Balance at January 1, 2018	\$	(461,390)
Net income		173,069
Change in nonadmitted assets		9,282
Other		1,175
Balance at December 31, 2018		(277,864)
Net income		96,949
Change in nonadmitted assets		135
Other		(3,012)
Balance at December 31, 2019	\$	(183,792)

See accompanying summary of significant accounting policies and notes to statutory financial statements.

Texas Windstorm Insurance Association

Statutory Statements of Cash Flows (Amounts in Thousands)

<i>Years ended December 31,</i>	2019	2018
Cash from operations:		
Premiums collected, net of reinsurance	\$ 280,264	\$ 294,900
Net investment loss	(23,324)	(29,059)
Miscellaneous income	43	279,673
Benefit and loss related payments	(111,977)	(307,283)
Commissions, expenses paid and aggregate write-ins for deductions	(234,448)	(183,022)
Net cash from operations	(89,442)	55,209
Cash from financing and miscellaneous sources:		
Principal and interest paid	(51,958)	(48,002)
Other cash (applied) provided	(116)	2,846
Net cash from financing and miscellaneous sources	(52,074)	(45,156)
Net change in cash and cash equivalents	(141,516)	10,053
Cash and cash equivalents, beginning of year	656,127	646,074
Cash and cash equivalents, end of year	\$ 514,611	\$ 656,127

See accompanying summary of significant accounting policies and notes to statutory financial statements.

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

Nature of Business

Based upon its statutory purpose under Chapter 2210, Tex. Ins. Code (the “Act”), the Texas Windstorm Insurance Association (the "Association") is an entity created by the Texas legislature with its primary statutory purpose being the provision of an adequate market for windstorm and hail insurance in the seacoast territory of Texas (“seacoast territory”). Chapter 2210 provides a method by which adequate windstorm and hail insurance may be obtained in certain designated portions of the seacoast territory.

The Association is intended to serve as a residual insurer of last resort for windstorm and hail insurance in the seacoast territory. The Association shall function in such a manner as to not be a direct competitor in the private market and to provide windstorm and hail insurance coverage to those who are unable to obtain that coverage in the private market.

Organization

The Association was established in 1971 by the Texas Legislature to provide wind and hail coverage to applicants unable to obtain insurance in the Texas seacoast territory from the private market. The Legislature’s action was a response to market constrictions along the Texas coast after several hurricanes. The Association is governed by Chapter 2210 of the Texas Insurance Code (Chapter 2210); however, it is not a state agency and does not receive funds from the general revenue.

The Association is a residual insurer of last resort and as such is not a direct competitor in the private market. The Association’s primary purpose is to provide an adequate market for windstorm and hail insurance in certain designated portions of the seacoast territory of Texas. The seacoast territory includes 14 first tier and 14 second tier coastal counties. The designated catastrophe area is that portion of the seacoast territory where the Commissioner of Insurance has found that windstorm and hail insurance is not reasonably available. It currently includes the entire first tier counties and a portion of Harris County (second tier). The specific designated catastrophe areas are: Aransas, Brazoria, Calhoun, Cameron, Chambers, Galveston, Jefferson, Kenedy, Kleberg, Matagorda, Nueces, Refugio, San Patricio and Willacy, inside the city limits and east of Highway 146, and the following portions of Harris County: La Porte, Morgan’s Point, Pasadena, Seabrook, and Shore Acres.

The Association operates as an insurance company by issuing policies, collecting premiums, and paying losses. The Association is required by law to use the net gain from operations each year to make payments to the CRTF, procure reinsurance, or use alternative risk mechanisms. The CRTF is an account maintained by the Texas Comptroller dedicated to funding the payment of Association catastrophe losses.

Association policies provide residential and commercial property coverage for losses resulting from windstorm or hail. No other perils are covered by Association policies. Applications for coverage, accompanied by the full annual premium, may be submitted to the Association through a property and casualty agent properly licensed through the Texas Department of Insurance (“TDI”). In order to be eligible for an Association policy, applicants and properties must meet certain criteria defined by the Texas Legislature:

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

- Applicants must have been denied coverage by at least one insurer in the private market.
- Properties must be located in the designated catastrophe area.
- Properties must be certified by the TDI as having been built to applicable building codes, with limited exceptions.
- Properties located in specified flood zones that were constructed, altered, remodeled, or enlarged after September 1, 2009 and that can obtain flood insurance through the National Flood Insurance Program must provide proof of flood insurance coverage.
- Properties must be in an insurable condition as specified by the Association in the Plan of Operation.

Texas Insurance Code Sections 2210.251 and 2210.258 - 2210.259 and the Association's Plan of Operation (28 TAC 5.4001 et seq.) outline the building code and inspection requirements for eligibility in the Association and provide for limited exceptions. In accordance with these sections, the Association requires a WPI-8 certificate of compliance on all structures constructed, altered, remodeled, enlarged, repaired, or to which additions have been made on or after January 1, 1988. To obtain a WPI-8, the TDI inspectors or the TDI-approved licensed professional engineers must inspect the property and certify that it is fully compliant with the windstorm building code.

Properties must be in an insurable condition to be eligible for Association coverage, i.e. in good repair with no unrepaired damage or hazardous conditions. The Association regularly inspects properties as part of its underwriting process to verify insurability. Properties may be inspected on-site by a vendor or remotely via high-quality aerial imagery. Inspections are used to determine the accuracy of rating information, discover any unrepaired damage, and identify any other conditions that affect the insurability of the property.

Approximately \$4,200,000 in funding was secured for the 2019 hurricane season. SB 900, passed by the 84th Texas Legislature, took effect during 2015, and changed the Association's funding structure. \$4,200,000 is sufficient to fund claims associated with 99% of all modeled hurricane seasons.

The Association's funding structure for the 2019 hurricane season is, in order;

- \$100,000 in CRTF funds
- \$500,000 in Class 1 public securities
- \$500,000 in Class 1 member assessments
- \$250,000 in Class 2 public securities
- \$250,000 in Class 2 member assessments
- \$250,000 in Class 3 public securities
- \$250,000 in Class 3 member assessments
- \$2,100,000 in total reinsurance, including both traditional reinsurance and catastrophe bonds

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

Class 1, 2, and 3 public securities will be repaid by Association premiums and surcharges on Association policies. Class 2 and 3 public securities, after a finding by the Commissioner of Insurance, may also be repaid by surcharges on coastal policyholders, if necessary.

Depopulation measures were introduced in the 84th Texas Legislature in 2015 authorizing assumption reinsurance agreements between the Association and the private market to facilitate depopulation. This allows private insurance companies interested in writing on the Texas coast to assume portions of the Association's book of business as of a point in time. Policyholders have the chance to opt-out of the assumption process.

The Association implemented the Assumption Reinsurance Depopulation Program ("Assumption Program") in 2016 and continued the Assumption Program through 2019. The Assumption Program requires participating insurers to work through agents to identify the policies that will receive assumption offers. A total of 1,866 and 3,967 policies were identified for assumption during 2019 and 2018, respectfully. Policyholders have until May 31, 2020 to opt out of the 2019 Assumption Program.

Basis of Accounting

The accompanying financial statements have been prepared on a statutory basis in accordance with accounting practices prescribed or permitted by the TDI. Prescribed statutory accounting practices include state laws, regulations and general administrative rules applicable to all insurance companies domiciled in the State of Texas and the National Association of Insurance Commissioners' ("NAIC") Accounting Practices and Procedures Manual. Permitted statutory practices include practices not prescribed but allowed by the TDI.

Reconciliations of net income and policyholders' deficit between the amounts reported in the accompanying financial statements (Texas basis) and NAIC statutory accounting practices ("SAP") follow:

<i>Years ended December 31,</i>	2019	2018
Net income, Texas basis	\$ 96,949	\$ 173,069
Effect of Texas prescribed practices	-	-
Effect of Texas permitted practices	-	-
Net income, NAIC SAP basis	\$ 96,949	\$ 173,069
<i>December 31,</i>	2019	2018
Statutory deficit, Texas basis	\$ (183,792)	\$ (277,864)
Effect of Texas prescribed practices	-	-
Effect of Texas permitted practices	(82,016)	(92,574)
Policyholders' deficit, NAIC SAP basis	\$ (265,808)	\$ (370,438)

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

The TDI has approved the permitted practice to allow the Association to admit the following restricted assets associated with the issuance of Series 2014 Pre-Event Class 1 Revenue Bonds (the “Bonds”) as of December 31, 2019 and 2018, respectively:

- \$82,016 and \$92,574 held in the obligation revenue fund for repayment of the Bonds.

The restrictions are primarily due to debt service reserves and use of proceeds only when a large hurricane event occurs. The permitted practice will last the life of the Bonds or until rescinded by the TDI at an earlier date.

Significant differences between statutory accounting practices and accounting principles generally accepted in the United States of America ("GAAP"), as they relate to the Association include the following:

- a) Certain assets designated as “non-admitted assets” are charged directly against surplus rather than capitalized and charged to income as used. These include certain past due member assessments, fixed assets, prepaid expenses and other assets.
- b) Unearned premiums and loss and loss adjustment expense (“LAE”) reserves are presented net of related reinsurance rather than on a gross basis as required under GAAP.
- c) The statements of cash flows represent cash balances and cash equivalents with initial maturities of one year or less rather than cash and cash equivalents with initial maturities of three months or less.

Use of Significant Estimates

The preparation of financial statements in accordance with statutory accounting practices prescribed or permitted by the TDI 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.

Reverse Repurchase Agreements

Reverse repurchase agreements are recorded in cash equivalents as the repurchase date is less than 90 days. Reverse repurchase agreements represent the purchase of a security with an agreement to resell.

Furniture, Equipment and Depreciation

Furniture and equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful life of 3-5 years. Amounts have been non-admitted.

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

Income Taxes

In 2010, the Association applied for and received a Private Letter Ruling (“PLR”) from the Internal Revenue Service (“IRS”). The PLR requested acknowledgement that the Association’s income is derived from an essential governmental function which accrues to a state or political subdivision and is therefore excluded from gross income under Section 115(1) of the Internal Revenue Code (“IRC”). On August 17, 2010, the IRS ruled that the Association performs an essential government function and that income from that function is excluded from gross income under IRC Section 115(1).

The Association had been filing form 1120-PC tax returns with the IRS as a property and casualty insurance company. Under the IRC the statute of limitations to be assessed additional taxes or to file amended tax returns is 3 years from the later of the due date of the return (including extensions) or the filing date of the return. There are existing net operating loss carryforwards in the open tax years that are not anticipated to be realized. As of December 31, 2019, the statute of limitations remains open for the 2016 to 2019 tax years. No further federal income tax impact is expected in the future.

Premiums

All policies issued by the Association have a maximum term of one year from date of issuance. Premiums earned are taken into income over the periods covered by the policies whereas the related acquisition costs are expensed when incurred. Premiums are generally recognized as revenue on a pro-rata basis over the policy term once the policy is effective. Unearned premiums, net of deductions for reinsurance, are computed on a pro-rata basis over the term of the policies.

Those premiums received for policies issued but not effective as of year-end are included in other liabilities within the Association's statutory statements of admitted assets, liabilities, surplus and other funds.

Those premiums received for policies which are not effective and not issued as of year-end are included in other liabilities within the Association’s statutory statements of admitted assets, liabilities, surplus and other funds.

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

Loss and Loss Adjustment Expense Reserves

Loss and LAE reserves are based upon claim estimates for (1) losses for claims reported prior to the close of the accounting period, (2) losses incurred but unreported prior to the close of the accounting period, and (3) expenses for investigating and adjusting claims. Such liabilities are necessarily based on assumptions and estimates and while management believes the amounts are adequate, the ultimate liability may be in excess of or less than the amount provided. The methods for making such estimates and for establishing the resulting liabilities are continually reviewed and any adjustments are reflected in the period determined.

Reinsurance

In the normal course of business, the Association seeks to reduce losses that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Depopulation ceded premiums are recognized as the ceded policies' premiums are earned.

Fair Value Measurements

Statement of Statutory Accounting Principles ("SSAP") No. 100R, Fair Value, requires disclosures of the aggregate fair value of all financial instruments, summarized by type of financial instrument, for which it is practicable to estimate fair value. SSAP No. 100R excludes obligations for pension benefits, substantively extinguished debt, insurance contracts, lease contracts, warranty obligations and rights, investments accounted for under the equity method and equity instruments issued by the entity. Accordingly, the aggregate fair value amounts presented herein do not necessarily represent the underlying value of the Association; similarly, care should be exercised in deriving conclusions about the Association's business or financial condition based on the fair value information presented herein.

The Association is required to categorize its assets and liabilities that are measured at fair value into the three-level fair value hierarchy. The three-level fair value hierarchy is based on the degree of subjectivity inherent in the valuation method by which fair value was determined. The three levels are defined as follows:

- Level 1 – Fair values are based on quoted prices in active markets for identical assets or liabilities that the Association has the ability to access as of the measurement date.
- Level 2 – Fair values are based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs that can otherwise be corroborated by observable market data.

Texas Windstorm Insurance Association

Summary of Significant Accounting Policies (Amounts in Thousands)

- Level 3 – Fair values are based on inputs that are considered unobservable where there is little, if any, market activity for the asset or liability as of the measurement date. In this circumstance, the Association has to rely on values derived by independent brokers or internally-developed assumptions. Unobservable inputs are developed based on the best information available to the Association which may include the Association's own data.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

1. Cash and Cash Equivalents

Cash and cash equivalents are as follows:

<i>December 31,</i>	2019		2018	
Cash	\$	209,840	\$	274,607
Cash equivalents:				
Reverse repurchase agreements		82,016		92,574
Money market mutual funds		222,755		288,946
Total cash equivalents		304,771		381,520
	\$	514,611	\$	656,127

Money Market Mutual Funds

The Association invests in money market mutual funds which are included in cash equivalents. The fair value of money market mutual funds was approximately \$222,755 and \$288,946 as of December 31, 2019 and 2018, respectively. The admitted value of money market mutual funds was \$222,755 and \$288,946 as of December 31, 2019 and 2018, respectively.

Reverse Repurchase Agreements

The Association invests in overnight reverse repurchase agreements with the Texas Treasury Safekeeping Trust Company (“TTSTC”). These invested funds were received from the issuance of bonds during 2014 and include debt service payments. The funds are held at the TTSTC to be used for debt service and for use when a catastrophic event occurs (See Note 12). The TTSTC’s minimum collateral required for overnight reverse repurchase investments is at least 100% for Treasuries; 101% for Agencies and U.S Instrumentalities and 102% for mortgage-backed securities. The fair value of reverse repurchase agreements was approximately \$82,016 and \$92,574 as of December 31, 2019 and 2018, respectively. The admitted value of reverse repurchase agreements was approximately \$82,016 and \$92,574 as of December 31, 2019 and 2018, respectively, and is included in cash and cash equivalents in the statutory statements of admitted assets, liabilities, surplus and other funds.

Repurchase agreements were Tri-Party during the years ended 2019 and 2018.

Original (flow) & residual maturity

	Fourth Quarter 2019	
	Maximum	Ending Balance
Overnight	\$ 82,016	\$ 82,016

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Fourth Quarter 2018			
	Maximum		Ending Balance
Overnight	\$	92,574	\$ 92,574

Securities acquired under repurchase agreements - sale

Fourth Quarter 2019			
	Maximum		Ending Balance
BACV	\$	82,016	\$ 82,016
Nonadmitted – subset of BACV		-	-
Fair value	\$	82,016	\$ 82,016

Book/Adjusting Carrying Value (“BACV”)

Fourth Quarter 2018			
	Maximum		Ending Balance
BACV	\$	92,574	\$ 92,574
Nonadmitted – subset of BACV		-	-
Fair value	\$	92,574	\$ 92,574

Securities acquired under repurchase agreements – sale by NAIC designation

<i>December 31, 2019</i>	None	NAIC 1	NAIC 2	NAIC 3	NAIC 4	NAIC 5	NAIC 6	Nonadmitted
Other invested assets – BACV	\$ -	\$ 82,016	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other invested assets – FV	-	82,016	-	-	-	-	-	-
Total assets – BACV	-	82,016	-	-	-	-	-	-
Total assets - FV	\$ -	\$ 82,016	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

<i>December 31, 2018</i>	None	NAIC 1	NAIC 2	NAIC 3	NAIC 4	NAIC 5	NAIC 6	Nonadmitted
Other invested assets – BACV	\$ -	\$ 92,574	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other invested assets – FV	-	92,574	-	-	-	-	-	-
Total assets – BACV	-	92,574	-	-	-	-	-	-
Total assets - FV	\$ -	\$ 92,574	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Proceeds Provided - Sale

Fourth Quarter 2019			
		Maximum	Ending Balance
Cash	\$	82,016	\$ 82,016
Securities (FV)		-	-
Securities (BACV)		-	-
Nonadmitted subset	\$	-	\$ -

Fourth Quarter 2018			
		Maximum	Ending Balance
Cash	\$	92,574	\$ 92,574
Securities (FV)		-	-
Securities (BACV)		-	-
Nonadmitted subset	\$	-	\$ -

Recognized forward resale commitment

Fourth Quarter 2019			
		Maximum	Ending Balance
Recognized forward resale commitment	\$	82,016	\$ 82,016

Fourth Quarter 2018			
		Maximum	Ending Balance
Recognized forward resale commitment	\$	92,574	\$ 92,574

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

2. Restricted Assets

Restricted assets summarized by restricted asset category. Certain assets below included in the subject to reverse repurchase category are held by the TTSTC and are restricted for use for debt service reserves and for when a catastrophic event occurs (See Note 12). These assets are invested in overnight reverse repurchase agreements.

Restricted Asset Category	Gross (Admitted & Nonadmitted) Restricted							Current Year				
	Current Year							Percentage				
	1	2	3	4	5	6	7	8	9	10	11	
	Total General Account (G/A)	G/A Supporting Restricted Assets (a)	Total Separate Account (S/A) Restricted Assets	S/A Assets Supporting G/A Activity (b)	Total (1 plus 3)	Total From Prior Year	Increase / (Decrease) (5 minus 6)	Total Non-admitted Restricted	Total Admitted Restricted (5 minus 8)	Gross (Admitted & Non-Admitted) Restricted to Total Assets (c)	Admitted Restricted to Total Admitted Assets (d)	
Subject to reverse repurchase	\$ 82,016	\$ -	\$ -	\$ -	\$ 82,016	\$ 92,574	\$ (10,558)	\$ -	\$ 82,016	13.44%	13.53%	
Total restricted assets	\$ 82,016	\$ -	\$ -	\$ -	\$ 82,016	\$ 92,574	\$ (10,558)	\$ -	\$ 82,106	13.44%	13.53%	

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

3. Furniture and Equipment

Furniture and equipment consist of the following:

<i>December 31,</i>	2019	2018
Furniture and equipment	\$ 541	\$ 470
Electronic data processing equipment and software	10,466	10,466
Leasehold improvements	1,858	1,858
	12,865	12,794
Less: accumulated depreciation	(12,212)	(12,016)
	653	778
Less: non-admitted furniture and equipment	(653)	(778)
	\$ -	\$ -

Depreciation and amortization expense was approximately \$196 and \$1,066 for the years ended December 31, 2019 and 2018, respectively.

4. Reinsurance

During 2019 and 2018, the Association entered into reinsurance agreements. These agreements reduce the amount of losses that can arise from claims under a general reinsurance contract known as a catastrophe aggregate excess of loss reinsurance agreement (“aggregate excess of loss”).

Aggregate Excess of Loss

Effective June 1, 2019, the reinsurance program is to indemnify the Association in respect of the liability that may accrue to the Association as a result of loss or losses under policies classified by the Association as property business, including, but not limited to residential, commercial and inland marine business, in force at the inception of this contract, or written or renewed during the term of this contract by or on behalf of the Association. The reinsurer shall be liable in the aggregate in respect of losses occurring during the term of this contract of 100% of the ultimate net loss over and above an initial ultimate net loss of \$2,100,000, subject to a limit of liability to the reinsurer of \$2,100,000.

Effective June 1, 2018, the reinsurance program is to indemnify the Association in respect of the liability that may accrue to the Association as a result of loss or losses under policies classified by the Association as property business, including, but not limited to residential, commercial and inland marine business, in force at the inception of this contract, or written or renewed during the term of this contract by or on behalf of the Association. The reinsurer shall be liable in the aggregate in respect of losses occurring during the term of this contract of 100% of the ultimate net loss over and above an initial ultimate net loss of \$2,000,000, subject to a limit of liability to the reinsurer of \$2,600,000. In 2017, the Association purchased a second season cover for \$800,000 in excess of \$2,000,000 of which 50% was placed. This cover was purchased to ensure that if an event occurred in 2017 and the

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

CRTF was depleted, additional reinsurance coverage would be available for the 2018 storm season. Due to the impact of Hurricane Harvey in 2017, the coverage became effective June 1, 2018. Reinsurance premiums related to the second season cover of \$12,805 were 100% earned during the year ended December 31, 2018 and is included in premiums ceded in the statutory statements of income.

Ceded reinsurance is treated as the risk and liability of the assuming companies; however, the reinsurance contracts do not relieve the Association from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Association. The Association evaluates the financial conditions of its reinsurers to minimize its exposure to significant losses from reinsurer insolvencies.

The Association has entered into quota share reinsurance agreements in relation to the Assumption Program (See Note 13).

The Association has unsecured reinsurance recoverables which exceed 3% of the Association's surplus with the following reinsurers as of December 31, 2019 and 2018 as a result of the Assumption Program:

Name of reinsurer	2019		2018	
Maison Insurance Company	\$	-	\$	2
Woodlands Insurance Company		-		5
United Property & Casualty Insurance Company		3		15
Weston Insurance Company		-		-
Total	\$	3	\$	22

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

The effect of reinsurance on premiums written and earned for the years ended December 31, 2019 and 2018 is as follows:

	2019		2018	
	Written	Earned	Written	Earned
Direct premium	\$ 372,017	\$ 381,571	\$ 395,552	\$ 409,954
Excess of loss ceded premium	(92,403)	(92,403)	(106,546)	(106,546)
Depopulation ceded premium	(1,691)	(1,691)	(1,893)	(1,893)
Net	\$ 277,923	\$ 287,477	\$ 287,113	\$ 301,515

Ceded premiums include premiums ceded to companies that assume policies pursuant to the Assumption Program (see Note 13).

As of December 31, 2019 and 2018, the Association had reinsurance recoverables of \$7 and \$5, respectively, of paid losses and LAE as a result of the Assumption Program and is included in other assets in the statutory statements of admitted assets, liabilities, surplus and other funds.

5. Unearned Premiums

Unearned premiums are reported net of ceded unearned premiums as follows:

<i>December 31,</i>	2019	2018
Gross unearned premiums	\$ 185,495	\$ 195,050
Ceded unearned premiums	-	-
	\$ 185,495	\$ 195,050

The amount of return commission that would have been due to reinsurers if they or the Association had cancelled the Association's excess of loss reinsurance agreement would have been \$0 as of December 31, 2019 and 2018.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

6. Loss and Loss Adjustment Expenses

The following table provides a reconciliation of the beginning and ending reserve balances, net of reinsurance recoverables, for losses and loss adjustment expenses:

<i>Years ended December 31,</i>	2019	2018
Beginning balance	\$ 200,858	\$ 415,213
Reinsurance recoverable	78	479
Beginning net balance	200,780	414,734
Incurred related to:		
Current loss year	26,454	19,442
Prior loss years	86,944	156,556
Losses and loss adjustment expense incurred	113,398	175,998
Paid related to:		
Current loss year	19,918	14,070
Prior loss years	125,130	375,882
Paid losses and loss adjustment expense	145,048	389,952
Ending net balance	169,130	200,780
Reinsurance recoverable	68	78
Ending balance	\$ 169,198	\$ 200,858

Current year changes in estimates of the cost of prior year losses and LAE affect the current year statutory statements of income. Increases in those estimates increase current year expense and are referred to as unfavorable development or prior year reserve shortages. Decreases in those estimates decrease current year expense and are referred to as favorable development or prior year reserve redundancies. Current year losses and LAE reflected on the statutory statements of income of \$113,398 reflect approximately \$86,944 unfavorable development of prior year estimates, primarily due to unfavorable development of 2017 accident year claims for Hurricane Harvey caused by a greater number and severity of supplemental payments on reopened claims occurring in 2019. Increases or decreases of this nature occur as the result of claim settlements and receipt and evaluation of additional information regarding unpaid claims. Recent development trends are also taken into account in evaluating the overall adequacy of reserves. During August 2017, the Association was impacted by Hurricane Harvey. Ultimate loss and LAE from Hurricane Harvey are estimated to be approximately \$1,700,000 as of December 31, 2019, an increase of \$90,000 from December 31, 2018 due to the severity of claims development. Due to the inherently uncertain process involving loss and LAE reserve estimates, the final resolution of the ultimate liability may be different from that anticipated at the reporting date. The appointed actuary for the Association has opined that the loss and LAE reserves as of December 31, 2019 and 2018 make a reasonable provision for the Association's claim liabilities.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

7. Statutory Fund

In 1993, the Texas legislature created the CRTF. At the end of each year and pursuant to administrative rules, the Association shall deposit the net gain from operations of the Association in excess of incurred losses, operating expenses, public security obligations, and public security administrative expenses into the CRTF and/or purchase reinsurance. Pursuant to Tex. Ins. Code §2210.259, a surcharge is charged on non-compliant structures insured by the Association, and these surcharges are deposited monthly into the CRTF.

When an occurrence or series of occurrences in a catastrophe area occurs, the Association shall pay losses in excess of premium and other revenue of the Association from available reserves of the Association and available amounts in the CRTF. Administrative rules adopted by the Commissioner of Insurance establish the procedures relating to the disbursement of money from the CRTF.

The Texas Comptroller of Public Accounts (“comptroller”) administers the CRTF in accordance with Tex. Ins. Code, Chapter 2210. All money, including investment income, deposited in the CRTF, are state funds to be held by the comptroller outside the state treasury on behalf of, and with legal title in, the TDI until disbursed as provided by the Tex. Ins. Code, Chapter 2210 and administrative rules adopted by the TDI under the Association’s Plan of Operation.

The CRTF may be terminated only by law. On termination of the CRTF, all assets of the CRTF revert to the state of Texas to provide funding for the mitigation and preparedness plan established under Tex. Ins. Code, §2210.454.

For the years ended December 31, 2019 and 2018, statutory fund costs were approximately \$52,641 and \$110,590, respectively, based on the direction of the TDI and based on its interpretation of the relevant statutes. The TDI’s directive required the Association to determine its net gain from operations based on catastrophe year losses, rather than calendar year reported losses. The Association is required to use the net gain from operations based on accident-year incurred losses of the Association to make payments to the CRTF, procure reinsurance, or use alternative risk financing mechanisms. Although amounts held in the CRTF are not presented as assets in the statutory statements of admitted assets, liabilities, surplus and other funds, once contributed to the CRTF, these funds will be held in trust with the TTSTC and will be available for the exclusive use of the Association to pay losses and expenses of the Association as permitted by law.

For the years ended December 31, 2019 and 2018, the CRTF held \$122,496 and \$5,986, respectively.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

In August 2017, Hurricane Harvey impacted the Texas coast and impacted the Association. Ultimate loss and LAE from Hurricane Harvey are estimated to be approximately \$1,700,000. The Act allows the Association to assess member companies relating to Class 1 member assessments up to \$500,000. A Class 1 member assessment was approved by the Commissioner of Insurance on May 25, 2018 for \$175,000, a second Class 1 member assessment was approved on August 20, 2018 for \$106,820, and a third Class 1 member assessment was approved on January 10, 2020 for \$90,000 for a combined total of \$371,820. As of December 31, 2019, \$279,621 has been collected from the first two assessments. The third assessment was billed on February 13, 2020 of which all was collected as of April 1, 2020. One insurance group has disputed their participation of a 2018 assessment in the amount of \$2,199, which has been non-admitted as of December 31, 2019 and 2018. In 2020, the Commissioner of Insurance overturned a ruling such that the insurance group is not subject to the 2018 assessment. The amount uncollected will be reallocated to other carriers and will be billed or returned to such carriers at a future date. Further assessments will be made as needed as Hurricane Harvey paid loss development matures. As of December 31, 2019 and 2018, the deficit of the Association is \$183,792 and \$277,864, respectively.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

8. Employee Benefit Plans

Defined Benefit Plan. The Association has a defined benefit pension plan (the “Plan”), which covers employees from their date of hire, if the employee is scheduled to work at least 1,000 hours in a twelve-month period. Pension benefits are based on years of service and the employee's compensation during the five highest consecutive years' earnings from the last ten years of employment. An employee's benefits vest 5 years from date of hire. The Association makes contributions to the Plan that comply with the minimum funding provisions of the Employee Retirement Income Security Act. Such contributions are included in general expenses. As of December 31, 2019 and 2018, the Association accrued in accordance with actuarially determined amounts with an offset to the pension cost accrual for the incremental asset amortization.

The following sets forth a summary of projected benefit obligations, plan assets, funded status, benefit costs and assumptions of the defined benefit pension plan as follows:

<i>December 31,</i>	2019	2018
<u>Change in Projected Benefit Obligations (PBO) (Underfunded):</u>		
Benefit obligation at beginning of year	\$ 22,937	\$ 23,457
Service cost	1,732	1,969
Interest cost	1,030	884
Actuarial loss (gain)	5,887	(2,795)
Benefits paid	(597)	(578)
Projected benefit obligation at end of year	30,989	22,937
<u>Change in Plan Assets:</u>		
Fair value of plan assets at beginning of year	16,171	15,598
Actual return on plan assets	3,614	(1,029)
Employer contributions	2,360	2,180
Benefits paid	(597)	(578)
Fair value of plan assets at end of year	21,548	16,171
Funded status	\$ (9,441)	\$ (6,766)

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

<i>December 31,</i>	2019		2018
<u>Funded Status:</u>			
Assets (non-admitted):			
Prepaid benefit costs	\$	-	\$ -
Total assets (non-admitted)		-	-
Liabilities recognized:			
Accrued benefit costs		2,554	2,890
Liability for pension benefits		6,887	3,876
Total liabilities recognized		9,441	6,766
Unrecognized liabilities as a component of net periodic benefit cost		-	-
Funded status	\$	(9,441)	\$ (6,766)
Accumulated benefit obligation	\$	27,626	\$ 20,319
<i>Years ended December 31,</i>	2019		2018
<u>Components of Net Periodic Benefit Costs:</u>			
Service costs	\$	1,731	\$ 1,969
Interest costs		1,031	884
Expected return on plan assets		(933)	(900)
Loss amortization		151	265
Prior service cost		44	44
Total net periodic benefit cost	\$	2,024	\$ 2,262

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

<i>Years ended December 31,</i>	2019	2018
<u>Amounts in unassigned funds (surplus) recognized as components of net periodic benefit cost:</u>		
Items not yet recognized as a component of net periodic cost – prior year	\$ 3,876	\$ 5,051
Net transition asset or obligation recognized	-	-
Net prior service cost or credit arising during the period	-	-
Net prior service cost recognized	(44)	(44)
Net loss (gain) arising during the period	3,206	(866)
Net gain recognized	(151)	(265)
Items not yet recognized as a component of net periodic cost – current year	\$ 6,887	\$ 3,876

<i>Years ended December 31,</i>	2019	2018
<u>Amounts in unassigned funds (surplus) expected to be recognized in the next fiscal year as components of net periodic benefit cost:</u>		
Amortization of net transition asset or obligation	\$ -	\$ -
Amortization of net prior service cost	44	44
Amortization of net loss	\$ 346	\$ 120

<i>Years ended December 31,</i>	2019	2018
<u>Amounts in unassigned funds (surplus) that have not yet been recognized as components of net periodic benefit cost:</u>		
Net transition asset or obligation	\$ -	\$ -
Net prior service cost	311	356
Net loss	\$ 6,576	\$ 3,520

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Pension Assumptions:

<i>December 31,</i>	2019	2018
Weighted-average assumptions used to determine net periodic benefit cost:		
Discount rate	4.50%	3.75%
Rate of compensation increase	2.50%	2.50%
Expected long-term rate of return of plan assets	5.50%	5.50%
Weighted-average assumptions used to determine projected benefit obligations:		
Weighted-average discount rate	3.50%	4.50%
Rate of compensation increase	2.50%	2.50%

The amount of accumulated benefit obligation for the defined benefit pension plan was approximately \$27,626 and \$20,319 as of December 31, 2019 and 2018, respectively.

Measurement Date

A measurement date of December 31, 2019 was used to determine the above.

Asset Allocation

The defined benefit pension plan asset allocation as of the measurement date presented as a percentage of total plan assets were as follows:

<i>December 31,</i>	2019	2018
Equity securities	36.0%	31.8%
Debt securities	59.0%	61.2%
Real estate	4.8%	5.1%
Other	0.2%	1.9%
	100.0%	100.0%

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

The investment policy of the Plan is to maximize the total return of the fund while maintaining a strong emphasis on preservation of capital. The total portfolio is expected to be less volatile than the market the vast majority of the time. The Plan assets are invested in a mix of equity and fixed income investments subject to target allocation ranges. The target allocation is to increase the percentage of fixed income investments depending on market conditions. Remaining funds not invested in the categories above are to be invested in short-term cash equivalents such as money market funds.

The long-term rate of return represents the expected average rate of return on the Plan assets based on the expected long-term asset allocation of the Plan. Several factors are considered, including historical market index returns, expectations of future returns in each asset classes, and the potential to outperform market index returns.

Future Payments

The following estimated future payments, which reflect expected future service, as appropriate, are expected to be paid in the years indicated:

<i>Years ending December 31,</i>	<i>Amount</i>
2020	\$ 695
2021	768
2022	861
2023	975
2024	1,085
2025 and thereafter	7,111

Planned Contributions

The Association expects to make contributions of \$2,568 during 2020.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Fair value measurements of Plan assets as of December 31, 2019 and 2018:

Fair Value Measurements at December 31, 2019				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Cash	\$ -	\$ 81	\$ -	\$ 81
Large cap equity	4,793	-	-	4,793
Small cap equity	650	-	-	650
Mid cap equity	1,468	-	-	1,468
International equity	-	2,402	-	2,402
Realty fund	-	1,300	-	1,300
Fixed income	-	10,852	-	10,852
Limited partnerships	-	-	2	2
Total plan assets	\$ 6,911	\$ 14,635	\$ 2	\$ 21,548

Fair Value Measurements at December 31, 2018				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Cash	\$ -	\$ 192	\$ -	\$ 192
Large cap equity	3,308	-	-	3,308
Small cap equity	478	-	-	478
Mid cap equity	1,054	-	-	1,054
International equity	-	1,464	-	1,464
Realty fund	-	1,059	-	1,059
Fixed income	-	8,614	-	8,614
Limited partnerships	-	-	2	2
Total plan assets	\$ 4,840	\$ 11,329	\$ 2	\$ 16,171

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Defined Contribution Plan. The Association has a defined contribution 401(k) plan available to eligible employees after six months of employment. The Association contributed approximately \$949 and 819 for the years ended December 31, 2019 and 2018, respectively.

9. Lease Commitments

The Association leases office space under a non-cancellable operating lease agreement which expires in 2022. Future minimum lease payments, by year and in the aggregate, under a non-cancellable operating lease with initial or remaining terms of one year or more consisted of the following at December 31, 2019:

<i>Years ending December 31,</i>		<i>Amount</i>
2020	\$	1,036
2021		1,062
2022		1,088
2023		-
2024 and thereafter		-
	\$	3,186

Rental expense under the non-cancelable operating lease was approximately \$1,422 and \$1,453 for the years ended December 31, 2019 and 2018, respectively.

10. Governance

Pursuant to SB 900 signed into law during 2015, the Board of Directors composition changed and now consists of nine members: three industry representatives from companies actively writing and renewing windstorm and hail insurance in the first tier coastal counties, three public members residing in the first tier coastal counties, and three non-coastal representatives who live more than 100 miles from the Texas coast. One of the public members must also be a property and casualty agent who is licensed under this code and is not a captive agent.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

11. Service Contract with Texas Fair Plan Association

During 2002, the Association entered into a service contract with the Texas Fair Plan Association ("TFPA") in which the Association is to be fully reimbursed for all expenditures, professional fees, consulting services, allocated employee time, lost investment income and other costs directly associated with the services provided by the Association on behalf of TFPA. During 2019 and 2018, the Association paid expenses for TFPA under its management contract and was reimbursed \$14,133 and \$13,787, respectively. As of December 31, 2019 and 2018, the Association incurred or paid expenses for which it has not been reimbursed of \$1,076 and \$1,029, respectively, on behalf of TFPA, and are included in other assets in the statutory statements of admitted assets, liabilities, surplus and other funds. This arrangement is subject to a written agreement which requires that balances be settled within 30 days.

12. Borrowed Money – Bonds Payable

The Texas Public Finance Authority (the "Authority" or the "Issuer") has issued the Bonds on behalf of the Association for the purposes of financing future costs in the amount of \$500,000. The Bonds are issued pursuant to a master resolution adopted by the Board of Directors of the Authority on September 24, 2014 (the "Master Resolution"), and a first supplemental resolution adopted by the Board of Directors of the Authority on September 24, 2014 (the "First Supplemental Resolution", and together with the Master Resolution, the "Resolutions"). The Bonds constitute the initial series of Class 1 Public Securities of the Authority secured and payable from Class 1 Pledged Revenues irrevocably pledged under the Resolutions. The Association has pledged the Class 1 Pledged Revenues to the Authority pursuant to a Financing and Pledge Agreement dated as of September 1, 2014 between the Authority and the Association.

The Bonds were issued on September 30, 2014 for \$500,000 of which \$318,600 and \$368,500 principal balance was outstanding as of December 31, 2019 and 2018, respectively, and is included in borrowed money – bonds and interest payable in the statutory statements of admitted assets, liabilities, surplus and other funds. The bonds mature July 1, 2024 and can be called by the Issuer beginning July 1, 2019. The Bonds outstanding bear stated and effective interest of 8.25%. Interest is payable semi-annually on January 1 and July 1 with the first payment made January 1, 2015. The Bonds are secured by the Association's net premium and other revenue which is used to fund the Debt Service and related accounts held by the TTSTC.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

There are various general and special covenants. The primary covenant, which exists as long as there are outstanding Class 1 Public Securities and Administrative Expenses are incurred, states that in the event the Association's Projected Net Coverage Revenues are less than 1.25 times the Obligations due in the next calendar year and 1.25 times the estimated amount of Administrative Expenses due in the next calendar year, the Association will undertake a plan of action or actions necessary to meet the required Projected Net Coverage Revenues. Another covenant, which exists as long as the Bonds are outstanding, states that the Association will maintain the Operating bank account subject to a deposit account control agreement to maintain a perfected security interest in the Net Premiums and Other Revenue held for the benefit of the Bondholders. The deposit account control agreement is activated upon default of certain debt covenants. As of December 31, 2019 and 2018, the Association is not in violation of these or any of the other various covenants.

The Bonds are subject to optional make-whole redemption, in whole or in part, at the option of the Authority, at the request of the Association prior to July 1, 2019 at a redemption price equal to the greater of (i) 100% of the principal amount of the Bonds to be redeemed or (ii) the sum of the present values of the remaining schedule payments of principal and interest on the Bonds to be redeemed (exclusive of interest accrued to the date fixed for redemption) discounted to the date of redemption on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at the Treasury Rate plus 100 basis points, plus in each case, accrued and unpaid interest on the Bonds being redeemed to the date fixed for redemption.

The Bonds are also subject to optional redemption prior to maturity on or after July 1, 2019, in whole or in part, at a redemption price equal to the principal amount of Bonds to be redeemed plus accrued interest to the date of redemption. The Association submitted a request to the Authority and the Commissioner of Insurance to make a partial redemption in the amount of \$45,000 with an anticipated redemption occurring in May 2020.

As of December 31, 2019, and 2018, the Bonds had no unamortized premium or discount. Bond issuance costs are expensed as incurred.

Interest expense incurred is recorded as an investment expense and was \$28,343 and \$32,303 for the years ended December 31, 2019 and 2018, respectively, and is included in net investment loss in the statutory statements of income. Interest expense of \$30,401 and \$34,205 was paid for the years ended December 31, 2019 and 2018, respectively. Interest payable was \$13,142 and \$15,201 as of December 31, 2019 and 2018, respectively, and is included in borrowed money – bonds and interest payable in the statutory statements of admitted assets, liabilities, surplus and other funds.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

Changes in borrowed money - bonds payable for the year ended December 31, 2019 is as follows:

Description	Bonds Outstanding January 1, 2019	Bonds Issued	Bonds Matured	Bonds Outstanding December 31, 2019
Bonds	\$ 368,500	\$ -	\$ 49,900	\$ 318,600

Changes in borrowed money - bonds payable for the year ended December 31, 2018 is as follows:

Description	Bonds Outstanding January 1, 2018	Bonds Issued	Bonds Matured	Bonds Outstanding December 31, 2018
Bonds	\$ 414,600	\$ -	\$ 46,100	\$ 368,500

The aggregate maturities for the next five years and thereafter is as follows:

<i>Years ending December 31,</i>	Amount
2020	\$ 54,000
2021	58,500
2022	63,300
2023	68,600
2024	74,200
On Demand	-
	\$ 318,600

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

13. Depopulation

Effective December 1, 2019, pursuant to measures introduced in the 84th Texas Legislature in 2015, the Association implemented year four of the Assumption Program. 1,866 policies were identified and approved by agents for possible transfer from the Association to the participating private market insurers with 1,549 policies remaining as of December 31, 2019. Policies will automatically transfer to participating companies on June 1, 2020. Policyholders may choose to remain with the Association by opting out of the Assumption Program by May 31, 2020. In connection with the Assumption Program, a 100% quota share reinsurance agreement was entered with two private market insurance companies effective December 1, 2019. Funds held by the Association under the Assumption Program as of December 31, 2019 will be settled at the end of the treaty period, June 1, 2020.

Effective December 1, 2018, pursuant to measures introduced in the 84th Texas Legislature in 2015, the Association implemented year three of the Assumption Program. 3,967 policies were identified and approved by agents for possible transfer from the Association to the participating private market insurers with 3,552 policies remaining as of December 31, 2018. Policies transferred to participating companies on June 1, 2019. Policyholders chose to remain with the Association by opting out of the Assumption Program by May 31, 2019. In connection with the Assumption Program, a 100% quota share reinsurance agreement was entered with two private market insurance companies effective December 1, 2018. Funds held by the Association under the Assumption Program as of December 31, 2018 were settled at the end of the treaty period, June 1, 2019.

As of December 31, 2019 and 2018, funds held by company under reinsurance treaties was \$179 and \$400, respectively, and is included in the statutory statements of admitted assets, liabilities, surplus and other funds.

During 2019 and 2018, the Association recognized ceded written premiums of \$1,691 and \$1,893, respectively, as a result of the Assumption Program.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

14. Commitments and Contingencies

The Association is subject to various investigations, claims and legal proceedings covering a wide range of matters that arise in the ordinary course of its business activities. Management believes that any liability that may ultimately result from the resolution of these matters in excess of the amounts provided will not have a material adverse effect on the financial position of the Association. These matters are subject to various uncertainties, and some of these matters may be resolved unfavorably to the Association.

The Association has obtained a \$500,000 committed line of credit with two of its primary financial institutions during 2019. The line of credit agreement was entered into July 1, 2019 subsequent to the Association's board of directors approval on May 7, 2019. No amounts were drawn against the line of credit. Issuance fees for the committed line of credit were \$500 and the Association pays the lenders a 0.4% commitment fee against the unused portion of the line of credit. The commitment originally matured May 27, 2020, however the line of credit was terminated by the Association as of December 26, 2019 without penalty.

15. Concentration of Credit Risk

The Association maintains deposits of cash in excess of federally insured limits with certain financial institutions. The Association has not experienced any losses in such accounts and believes they are not exposed to any significant credit risk on cash.

The Association writes windstorm and hail coverage primarily in the 14 counties along the Texas coast in which it has approximately \$61,000,000 and \$64,000,000 of insurance exposure as of December 31, 2019 and 2018, respectively.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

16. Nonadmitted Assets

Nonadmitted assets consisted of the following:

<i>December 31,</i>		2019		2018
Prepaid expenses and receivables	\$	1,245	\$	1,255
Member assessment receivable		2,199		2,199
Furniture and equipment		653		778
Total nonadmitted assets	\$	4,097	\$	4,232

17. Fair Value Measurements

The following table reflects the fair values and admitted assets and liabilities that are financial instruments. The fair values are also categorized into the three-level fair value hierarchy. Cash and cash equivalents are the only financial instruments held by the Association. The investment strategy for the Association is to hold highly liquid cash and cash equivalents for funding catastrophe events. The Association does not believe that the assets stated at NAV have any significant restrictions to liquidate or to be sold for less than NAV.

Fair Value Measurements at December 31, 2019 Using:

	Aggregate Fair Value	Net Asset Value	Admitted Assets	Level 1	Level 2	Level 3
Cash	\$ 209,840	\$ -	\$ 209,840	\$ 209,840	\$ -	\$ -
Cash equivalents*	82,016	222,755	304,771	82,016	-	-
	\$ 291,856	\$ 222,755	\$ 514,611	\$ 291,856	\$ -	\$ -

Fair Value Measurements at December 31, 2018 Using:

	Aggregate Fair Value	Net Asset Value	Admitted Assets	Level 1	Level 2	Level 3
Cash	\$ 274,607	\$ -	\$ 274,607	\$ 274,607	\$ -	\$ -
Cash equivalents*	92,574	288,946	381,520	92,574	-	-
	\$ 367,181	\$ 288,946	\$ 656,127	\$ 367,181	\$ -	\$ -

* In accordance with SSAP 100R, certain investments that were measured at NAV have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation to the line items presented in the statutory statements of admitted assets, liabilities, surplus and other funds.

Texas Windstorm Insurance Association

Notes to Statutory Financial Statements (Amounts in Thousands)

18. Reconciliation with Annual Statement

There were no differences between the 2019 annual statement and 2018 annual statement as filed with the TDI and the 2019 and 2018 audited statutory financial statements.

19. Subsequent Events

The Association has evaluated subsequent events occurring after December 31, 2019, the date of the most recent statutory statements of admitted assets, liabilities, surplus, and other funds through April 23, 2020, the date the statutory financial statements were issued.

In June of 2019, the Association increased loss and loss adjustment expense reserves related to Hurricane Harvey in the amount of \$90,000. In accordance with the Texas Insurance Code Chapter 2210, the Association is permitted to assess member companies to fund these additional loss amounts with the approval of the Commissioner of the TDI (“the Texas Commissioner”). The Association recorded the member assessment revenue of \$90,000 and the related assessment receivable as of December 31, 2019 and received approval from the Texas Commissioner on January 10, 2020. The amounts from the assessment have been collected as of April 1, 2020 (See Note 7).

As discussed in Note 12 (Borrowed Money – Bonds Payable), the outstanding Texas Public Finance Authority Class 1 Revenue Bonds issued on behalf of the Association, are subject to optional redemption prior to maturity on or after July 1, 2019 at a redemption price equal to the principal amount of bonds to be redeemed plus accrued interest to the date of redemption. On February 18, 2020, the Association Board of Directors approved an early redemption in the amount of \$45,000 and directed Association staff to request approval from the Texas Commissioner. On February 24, 2020, the Association received approval from the Texas Commissioner to redeem the requested \$45,000 of bond principal. The redemption is anticipated to be completed during the second quarter of 2020.

The Association does not believe any subsequent events have occurred that would require further disclosure or adjustment to the statutory financial statements.

Texas Windstorm Insurance Association

Summary Investment Schedule December 31, 2019 (Amounts in Thousands)

Investment categories	Gross Investment Holdings *		Admitted Assets as Reported in the Annual Statement **	
	Amount	%	Amount	%
Long- Term Bonds (Schedule D, Part 1):				
U.S. Governments	\$ -	-	\$ -	-
All other governments	-	-	-	-
U.S. states, territories and possessions, etc. guaranteed	-	-	-	-
U.S. political subdivisions of states, territories, and possessions, guaranteed	-	-	-	-
U.S. special revenue and special assessment obligations, etc. non-guaranteed	-	-	-	-
Industrial and miscellaneous	-	-	-	-
Hybrid securities	-	-	-	-
Parent, subsidiaries and affiliates	-	-	-	-
SVO identified funds	-	-	-	-
Unaffiliated bank loans	-	-	-	-
Total long-term bonds	-	-	-	-
Preferred stocks (Schedule D, Part 2, Section 1):				
Industrial and miscellaneous (Unaffiliated)	-	-	-	-
Parent, subsidiaries and affiliates	-	-	-	-
Total preferred stocks	-	-	-	-
Common stocks (Schedule D, Part 2, Section 2):				
Industrial and miscellaneous Publicly traded (Unaffiliated)	-	-	-	-
Industrial and miscellaneous Other (Unaffiliated)	-	-	-	-
Parent, subsidiaries and affiliates Publicly traded	-	-	-	-
Parent, subsidiaries and affiliates Other	-	-	-	-
Mutual funds	-	-	-	-
Unit investments trusts	-	-	-	-
Closed-end funds	-	-	-	-
Total common stocks	-	-	-	-
Mortgage loans (Schedule B):				
Farm mortgages	-	-	-	-
Residential mortgages	-	-	-	-
Commercial mortgages	-	-	-	-
Mezzanine real estate loans	-	-	-	-
Total mortgage loans	-	-	-	-
Real Estate (Schedule A):				
Properties occupied by company	-	-	-	-
Properties held for production of income	-	-	-	-
Properties held for sale	-	-	-	-
Total real estate	-	-	-	-

See accompanying independent auditors' report on supplemental information.

Texas Windstorm Insurance Association

Summary Investment Schedule December 31, 2019 (Amounts in Thousands)

Investment categories	Gross Investment Holdings *		Admitted Assets as Reported in the Annual Statement **	
	Amount	%	Amount	%
Cash, cash equivalents and short-term investments:				
Cash (Schedule E, Part 1)	209,840	40.78	209,840	40.78
Cash equivalents (Schedule E, Part 2)	304,771	59.22	304,771	59.22
Short-term investments (Schedule DA)	-	-	-	-
Total cash, cash equivalents and short-term investments	514,611	100.00	514,611	100.00
Contract loans	-	-	-	-
Derivatives (Schedule DB)	-	-	-	-
Other invested assets (Schedule BA)	-	-	-	-
Receivables for securities	-	-	-	-
Securities Lending (Schedule DL, Part 1)	-	-	-	-
Other invested assets (Page 2, Line 11)	-	-	-	-
Total invested assets	\$ 514,611	100.00	\$ 514,611	100.00

*Gross investment holdings as valued in compliance with the NAIC Accounting Procedures Manual.

** The Association has no securities lending reinvested collateral at December 31, 2019.

See accompanying independent auditors' report on supplemental information.

Texas Windstorm Insurance Association

Supplemental Investment Risk Interrogatories

December 31, 2019

(Amounts in Thousands)

- 1) Reporting entity's total admitted assets as reported in the accompanying financial statements. \$ 606,117

Questions 2 through 19 are not applicable.

- 20) Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

	At Year-End		At End of Each Quarter		
	Amount	Percentage of Total Admitted Assets	1 st Qtr	2 nd Qtr	3 rd Qtr
Reverse repurchase agreements	\$ 82,016	13.53%	\$ 97,958	\$ 106,359	\$ 61,591

Questions 21 through 23 are not applicable.

See accompanying independent auditors' report on supplemental information.

Texas Windstorm Insurance Association

Reinsurance Interrogatories

December 31, 2019

(Amounts in Thousands)

7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)? YES[] NO [X]

7.2 If yes, indicate the number of reinsurance contracts containing such provisions. N/A

7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)? YES[] N/A [X]

9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:

(a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;

(b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity; or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;

(c) Aggregate stop loss reinsurance coverage;

(d) A unilateral right by either party (or both parties) to commute the reinsurance contract, whether conditional or not, except for such provisions which are only triggered by a decline in the credit status of the other party;

(e) A provision permitting reporting of losses, or payment of losses, less frequently than a quarterly basis (unless there is no activity during the period); or

(f) Payment schedule, accumulating retentions from multiple years or any features inherently designed to delay timing of the reimbursement to the ceding entity.

YES[] NO [X]

See accompanying independent auditors' report on supplemental information.

Texas Windstorm Insurance Association

Reinsurance Interrogatories

December 31, 2019

(Amounts in Thousands)

9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), for which, during the period covered by the statement, it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; excluding cessions to approved pooling arrangements or to captive insurance companies that are directly or indirectly controlling by, or under control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member where:

(a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or

(b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in a separate reinsurance contract?

YES [] NO [X]

9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:

N/A

9.4 Except for transactions meeting the requirements of paragraph 31 of SSAP No. 62R, Property and Casualty Reinsurance, has the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:

(a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles ("SAP") and as a deposit under generally accepted accounting principles ("GAAP"); or

(b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?

YES [] NO [X]

9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated differently for GAAP and SAP.

N/A

See accompanying independent auditors' report on supplemental information.