

# WTC Captive Insurance Company, Inc.

Independent Auditors' Report, Financial Statements  
and Additional Information

As of and for the Years Ended  
December 31, 2013 and 2012



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*Certified Public Accountants and Consultants*

**WTC Captive Insurance Company, Inc.**  
**Independent Auditors' Report, Management's Discussion and Analysis, Financial Statements,**  
**and OMB Circular A-133 Report**  
**As of and for the Years Ended December 31, 2013 and 2012**

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**Independent Auditors' Report**

To the Board of Directors of  
WTC Captive Insurance Company, Inc.

We have audited the accompanying financial statements of WTC Captive Insurance Company, Inc. ("the Company"), which comprise the statements of net position as of December 31, 2013 and 2012, the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of 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 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the 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 Company'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 financial statements.

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

**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of WTC Captive Insurance Company, Inc. as of December 31, 2013 and 2012, and the activities and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.



## Other Matters

The accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis on pages 3-13 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## Report on Other Legal and Regulatory Requirements

In accordance with *Government Auditing Standards*, we have also issued our report dated March 10, 2014 on our consideration of the Company's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. This schedule is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Saslow Lufkin & Buggy, LLP*

March 10, 2014  
Avon, CT

## **WTC Captive Insurance Company, Inc. Management's Discussion and Analysis**

The following discussion and analysis of WTC Captive Insurance Company, Inc.'s ("WTC Captive" or the "Company") financial performance provides an overview of the Company's financial activities as of and for the year ended December 31, 2013. It should be read in conjunction with the financial statements, which begin on page 14.

WTC Captive is a not-for-profit corporation formed in the State of New York in response to the events of September 11, 2001. WTC Captive was established pursuant to the Consolidated Appropriations Resolution, 2003, P.L. 108-7, signed by President Bush on February 20, 2003, and corollary enabling State of New York legislation. WTC Captive was incorporated on July 1, 2004; it was funded by the Federal Emergency Management Agency ("FEMA"), licensed as a captive insurance company by the New York State Department of Financial Services ("NYSDFS") and commenced operations on December 3, 2004.

Pursuant to a liability insurance contract (the "Contract"), WTC Captive provides specified coverage against certain third-party claims made against New York City (the "City") and approximately 145 contractors and subcontractors (collectively, "Additional Named Insureds") working on the City's FEMA-funded debris removal project. WTC Captive coverage includes general liability, environmental liability, professional liability and marine liability. Coverage is provided on both an excess of loss and first dollar basis, depending on the line of coverage. The effective dates of the Contract are with respect to exposures occurring from September 11, 2001 (post-collapse) through August 30, 2002. This period is referred to as the "exposure period." This is the only insurance contract that has or will be issued by WTC Captive, and all of the Company's business activities relate to its obligations under the Contract.

The insureds of the WTC Captive were sued in numerous cases alleging some harm during the exposure period as defined by the Contract. At the peak, there were over 10,000 plaintiffs who had sued one or more of the WTC Captive's insureds alleging exposure to toxins at the World Trade Center site following the terrorist attacks on 9/11. Thousands of additional claims were pending on behalf of the spouses of those claiming exposure. The WTC Captive defended nearly all of these cases under the terms of its insurance policy.

The cases, all venued in the US District Court for the Southern District of New York, were organized by the court into three separate dockets, or "Master Calendars" ("MC"). The primary litigation against insureds of the WTC Captive was in the "debris removal" docket, MC 100 ("MC 100"), with allegations by workers involved in the rescue, recovery, and debris removal operations associated with the attacks on the World Trade Center. Additional litigation against WTC Captive's insureds was included in the "off site" docket, MC 102 ("MC 102"), which largely consists of claims of building cleaners who were responsible for removing dust and debris from inside office buildings near the World Trade Center. Finally, a smaller group of plaintiffs made allegations regarding both on-site and off-site work; these claims were placed in the "straddle" docket, MC 103 ("MC 103").

On June 23, 2010, the Settlement Process Agreement, as Amended ("Amended SPA") was reached with attorneys representing over 10,000 plaintiffs and approved by Judge Alvin Hellerstein, and by November 2010, the WTC Captive determined, based on information provided by the Amended SPA administrator, that the minimum required 95% of plaintiffs had evidenced an intention to opt in to the agreement.

The Amended SPA contained several financial components to be contributed by the WTC Captive: i) a base settlement contribution of \$625 million; ii) opt-in bonus payments of 2% of the settlement amount for every one percent in excess of the 95% opt-in requirement, and if the opt-in threshold exceeds 98%, additional opt-in bonus payments of one-fifth of one percent (0.20%) for every tenth of one percent (0.10%) above the 98% opt-in rate. At a 100% opt-in rate the bonus payments would total 10% of the settlement amount; iii) a contingent payment structure of up to \$25 million; iv) a contribution of \$3.5 million towards the costs of administering the settlement; and v) contribution of the WTC Captive's interest in an underlying marine insurance policy. In 2011 the parties signed a settlement agreement concerning this underlying marine policy and on June 9, 2011, \$28 million was transferred to the Amended SPA settlement account.

## **WTC Captive Insurance Company, Inc. Management's Discussion and Analysis**

On January 5, 2011, the parties to the settlement signed the affirmation of final settlement, triggering the claims evaluation process and beginning the process of distributing payments. The first round of payments under the settlement was made on January 27, 2011. On March 4, 2011, WTC Captive determined that the opt-in percentage to the settlement exceeded 96%. This triggered a bonus payment of \$12.5 million that WTC Captive deposited into the settlement account on March 7, 2011.

The WTC Captive's insureds have appealed a series of rulings and actions by Judge Hellerstein relative to the settlement, including his determination that the involuntary dismissal of plaintiffs should reduce the denominator for the opt-in calculations, which would result in greater opt-in "bonus" payments under the settlement. On September 8, 2011, Judge Hellerstein issued a final order concerning calculation of the settlement opt-in percentage, updating his December 30, 2010 order on the matter. The WTC Captive continues to disagree with the logic and calculation in this ruling. However, \$42.5 million has been placed in a separate account pending a ruling on the matter by the Second Circuit. In light of this separation of funds, the Company was able to obtain a stay of the September 8, 2011 order, pending appeal.

The appeal on the opt-in percentage has been consolidated with an appeal regarding the first contingent payment. As part of the Amended SPA, the WTC Captive agreed to make payments of up to \$5 million per year for each of the first five years following the affirmation of the final settlement dependent upon a number of factors, including the number of new claims filed and the cost of resolving those claims. The first date for review of those criteria was January 5, 2012. Upon advice of counsel, there was no payment due because the number of post-settlement claims exceeded the threshold for payment as set forth in the Amended SPA. However, Judge Hellerstein issued an order dated July 13, 2012 interpreting the contingent payment terms of the Amended SPA such that the first contingent payment of \$5 million, calculated based on the number of new claims filed each year, was to be paid notwithstanding previous agreement by the parties that no such payment was due. Judge Hellerstein also directed that plaintiffs' counsel should not receive any fee on the contingent payments. The WTC Captive continues to dispute the issue and has taken an appeal, and plaintiffs' counsel has appealed the ruling on fees. The amount in question was deposited into the separate account pending the results of the appeal, and the order was stayed.

The issue returned in January 2013 when the second contingent payment was due. Based on calculations according to the WTC Captive's appellate position, \$3.8 million was due in 2013 out of the possible \$5 million in contingent payments under the Amended SPA. The parties reached agreement that the WTC Captive would pay the actual plaintiffs' portion of this \$3.8 million, or about \$2.85 million, according to the terms of the Amended SPA, setting aside the attorneys' fees and the remaining \$1.2 million to be addressed according to the results of the appeal. The agreement is without prejudice to either side's position in the appeal. As a result, \$3.8 million was placed into the settlement account on January 15, 2013. The amount agreed to for individual plaintiffs, \$2.85 million, was paid out on January 16, 2013 according to instructions from the Allocation Neutral, while fees of about \$950,000 subject to appeal remained in the settlement account. The remaining \$1.2 million of the \$5 million was placed into the separate account pending results of the appeal. In total, about \$48.7 million has been placed in a separate account relative to the bonus and contingent payment appeals. Briefing is complete on the consolidated appeals and oral argument was presented in April 2013. Corporate counsel argued on behalf of the WTC Captive and its insureds, and the questions focused on issues of contract interpretation. A ruling is expected in 2014.

In January 2014, the third contingent payment was due. Under the terms of the Amended SPA, the full \$5 million was owed. On February 3, 2014, WTC Captive paid the actual plaintiffs' portion of this \$5 million, or about \$3.8 million, according to the terms of the Amended SPA, setting aside the attorneys' fees of about \$1.2 million to be addressed according to the results of the appeal.

## **WTC Captive Insurance Company, Inc. Management's Discussion and Analysis**

Apart from the settlement described above, there were 100 cases naming at least one WTC Captive insured as a defendant, not including various cases in which the plaintiff has filed a notice of withdrawal seeking dismissal in favor of the re-opened Victim Compensation Fund ("VCF"). These cases were all in active discovery in 2012, and the WTC Captive sought to resolve them where possible at appropriate amounts. While plaintiffs' counsel was very interested in pursuing settlement discussions, Judge Hellerstein's ambitious discovery schedule put pressure on the parties. WTC Captive management maintained a steady pace throughout 2012 with regular meetings with plaintiffs' counsel. Ninety-two cases were settled in principle in 2012, 87 of them including significant claims of respiratory injury, the other five were non-respiratory cases as noted below. Total settlement value for those 87 cases is approximately \$20 million. In 2013, the WTC Captive continued to pursue resolution of outstanding claims, by motion practice and settlement. Three claims were dismissed by Judge Hellerstein, either based on the statute of limitations or for failure to comply with discovery obligations and court orders. Five claims were settled in 2013, two alleging primarily respiratory injury and three non-respiratory cases. The 2013 respiratory settlements totaled just under \$1 million.

The WTC Captive inherited the defense of several orthopedic injury cases against various insureds as a result of its settlements with the Liberty and London GL carriers. During the course of 2011, the WTC Captive awaited the deadline for the re-opened VCF to see what plaintiffs would remain rather than actively pursuing settlements. The WTC Captive settled five of these non-respiratory cases in principle, including one through mediation, during 2012. The total settlement value of these five cases was \$1.2 million. As noted above, three additional non-respiratory cases were settled in 2013, each of these went through mediation. The total value of the 2013 non-respiratory settlements was \$6.8 million.

The total value of 2013 settlements was \$7.7 million. Several claims settled in principle in 2012 were finalized and paid in 2013, and with a previous settlement in principle paid in January 2014 there are no incomplete settlements. Total settlement cost for the claims resolved in 2012 and 2013 was \$29 million, of which \$21 million was for respiratory cases and the remaining \$8 million was for non-respiratory cases. One new case was filed in 2012, but has not been in active discovery and remains open.

Under the terms of its Bylaws, grant agreements and the Contract, the WTC Captive is authorized, and at certain times required, to evaluate the purchase of assumption reinsurance. Assumption reinsurance would provide the Company the ability to reinsure some or all of its obligations. With the resolution of essentially all claims against the Company's insureds, together with the reopening of the VCF, WTC Captive undertook its first such evaluation in 2013. Through the summer, WTC Captive undertook a competitive process to secure assumption reinsurance proposals. A Request for Proposal was developed, and eight global insurers were invited to compete for the opportunity. Two proposals were received, with one of the proposals offering terms most closely aligned with the Company's goals. These goals are straightforward: increased limits of financial protection for all insureds within a transaction structure that benefits all insureds while harming none; comparable coverage terms to the existing Contract; true assumption reinsurance that assigns all rights and obligations of the WTC Captive under the Contract to the new insurer; a demonstrated understanding by the assuming insurer of the unique provisions of the Contract; and an insurer who can provide long-term financial security for the WTC Captive's insureds. While the transaction was under regulatory review by NYSDFS and FEMA in November 2013, concerns raised by some members of Congress and by advocates for first responders put the transaction on hold. The transaction remains pending regulatory approval.

## **WTC Captive Insurance Company, Inc. Management's Discussion and Analysis**

### ***Financial Highlights***

The Company accounts for the Contract utilizing deposit accounting. Deposit accounting is used to account for insurance contracts that do not transfer insurance risk and its guidelines affect how certain expenditures of the Company are recognized in its financial statements. It is important for a reader of these financial statements to understand deposit accounting to appreciate fully the financial performance of the Company. Deposit accounting is explained in further detail throughout the Management's Discussion and Analysis and the notes to the audited financial statements.

Pursuant to a series of agreements, WTC Captive received funding of \$999.9 million on December 3, 2004. Funds amounting to \$899.9 million were recorded directly to "deposit liability." The Company's Board of Directors approved the designation of \$100 million to satisfy the capital and surplus requirements of the NYSDFS, as required by Section 7004 of the New York Insurance Law, Article 70. The designation of \$100 million was based on an assessment of factors that would impact amounts designated as capital, primarily related to potential changes in the market value of the investment portfolio, which are charged directly to operations, and the potential for interest accretion and operating expenses to exceed gross investment income in a given year, as more fully described below. WTC Captive holds the amounts designated to satisfy capital and surplus as a liability, "residual liability" on its *Statements of Net Position*. Amounts designated to satisfy capital and surplus requirements are held as a liability, rather than as residual net assets, due to provisions of the Company's organizational documents that require the Company to return funding that remains, if any, after all obligations have been satisfied, as defined by and according to the terms of the organizational documents. Additionally, any net gain or loss from operations will directly impact the Company's residual liability designated to satisfy capital and surplus requirements. As such, the net operating losses recorded for the years ended December 31, 2013, 2012 and 2011, respectively, have been reflected within the residual liability on the Company's *Statements of Net Position*. Designation of funds to satisfy capital and surplus requirements does not restrict the ability of the Company to use such funds to satisfy its obligations.

The Company reported net operating losses of \$(8.4 million), \$(7.1 million) and \$(33.1 million) for the years ended December 31, 2013, 2012 and 2011, respectively. The net operating losses for the years ended December 31, 2013 and 2012, respectively, were attributable to the excess of the sum of operating expenses and the recognition of accretion expense, which was netted against investment income, over the amount of investment income. The net operating loss for the year ended December 31, 2011 was primarily attributable to the recognition of a \$27.3 million life-to-date interest accretion expense adjustment (a component of the overall interest accretion expense totaling \$34.2 million).

For all years, the Company's sole source of income was investment income derived from the amount of invested assets.

### ***Overview of the Financial Statements***

This annual financial report consists of Management's Discussion and Analysis (this section) and basic financial statements. Basic financial statements consist of: *Statements of Net Position*, *Statements of Activities*, *Statements of Cash Flows* and *Notes to the Financial Statements*. WTC Captive is subject to accounting standards promulgated by the Governmental Accounting Standards Board as applied by the City.

The *Statements of Net Position* provide an indication of WTC Captive's financial status. These statements provide information on the ability of WTC Captive to meet its obligations, primarily related to issuance of the Contract described above. As described above, no net assets are reported by the Company due to provisions of the Company's organizational documents that require the Company to return funding that remains, if any, after all obligations have been satisfied.



**WTC Captive Insurance Company, Inc.**  
**Management's Discussion and Analysis**

The *Statements of Activities* report all of the revenues and expenses during the indicated time period. Any net operating gain or loss recognized is closed into the residual liability account presented on the *Statements of Net Position*. WTC Captive reports information using the full accrual basis of accounting commonly used by private-sector companies.

The *Statements of Cash Flows* report the cash provided from and used by operating and investing activities. Sources and uses of cash are shown on a direct basis. Additionally, a reconciliation of net operating loss to net cash provided from operating activities is provided on an indirect basis.

*Notes to the Financial Statements* provide additional information and schedules that are essential to a complete understanding of the information provided in the financial statements, including discussion related to the Company's use of deposit accounting with respect to the Contract issued by the Company, as discussed further in Notes 2 and 5.

The following is a summary of WTC Captive's *Statements of Net Position*:

<i>(Dollars in thousands)</i>	<b>2013</b>	<b>December 31, 2012</b>	<b>2011</b>
	<hr/>	<hr/>	<hr/>
<b>Assets</b>			
Cash and investments	\$ 327,724	\$ 351,559	\$ 402,325
Cash and investments - restricted	4,077	4,608	384,791
Total cash and investments	<hr/> 331,801	<hr/> 356,167	<hr/> 787,116
Other assets	121	976	1,058
Other assets - restricted	-	-	2
Total other assets	<hr/> 121	<hr/> 976	<hr/> 1,060
Total assets	<hr/> <hr/> \$ 331,922	<hr/> <hr/> \$ 357,143	<hr/> <hr/> \$ 788,176
<b>Liabilities</b>			
Debris removal settlement liability	\$ 4,077	\$ 4,608	\$ 384,793
Accrued liabilities	105	270	554
Non-current liabilities			
Deposit liability	197,808	213,887	257,313
Residual liability	<hr/> 129,932	<hr/> 138,378	<hr/> 145,516
Total liabilities	<hr/> <hr/> \$ 331,922	<hr/> <hr/> \$ 357,143	<hr/> <hr/> \$ 788,176

**WTC Captive Insurance Company, Inc.**  
**Management's Discussion and Analysis**

Nearly all of WTC Captive's assets are held as either cash or investments. As of December 31, 2013, these assets totaled approximately \$331.8 million. Other assets of the Company included \$82 thousand of accrued investment income. The liabilities of the Company included the debris removal settlement liability of \$4.1 million, the deposit liability of \$197.8 million and a residual liability of \$129.9 million. The net loss from operations, amounting to \$(8.4 million), \$(7.1 million) and \$(33.1 million) for the years ended December 31, 2013, 2012 and 2011, respectively, have been reflected within the residual liability. Net losses from operations reduce total liabilities of the Company, while net gains increase total liabilities. This is due to the fact that the Contract and provisions of the Company's organizational documents require the Company to utilize all of its resources to satisfy obligations under the Contract, as necessary. Any funds that remain after all obligations have been satisfied must be returned as defined by and according to the terms of the organizational documents. Hence, to the extent that the Company has net gains from operations, it has additional resources either to satisfy obligations under the Contract or to return pursuant to the terms of the organizational documents.

The composition of cash and investments at December 31, 2013, 2012 and 2011, are as follows:

<i>(Dollars in thousands)</i>	<u><b>2013</b></u>	<u><b>2012</b></u>	<u><b>2011</b></u>
Cash and cash equivalents	\$ 290,914	\$ 6,272	\$ 32,675
Cash and cash equivalents - restricted	4,077	4,608	384,291
Total	<u>294,991</u>	<u>10,880</u>	<u>416,966</u>
Fixed maturity securities, at fair value	36,810	345,287	369,650
Fixed maturity securities, at fair value - restricted	-	-	500
Total	<u>36,810</u>	<u>345,287</u>	<u>370,150</u>
Total cash and investments	<u><u>\$ 331,801</u></u>	<u><u>\$ 356,167</u></u>	<u><u>\$ 787,116</u></u>

WTC Captive's Board of Directors' approved investment policy statement outlines the Company's investment objectives, policies and procedures, among other matters. WTC Captive's broad investment objective emphasizes the preservation of invested assets and maintenance of sufficient liquidity to meet the Company's obligations as defined by the Contract. As a secondary objective, the Company's investment policy seeks to achieve a total return that exceeds, after management fees, the benchmarks approved by its Board of Directors.

BlackRock Financial Management, Inc. ("BlackRock") has served as the Company's investment manager since 2005. Early in its tenure, BlackRock split the Company's investment funds equally between a Liquidity portfolio and a Short Duration portfolio. The Liquidity portfolio is benchmarked against the Bank of America Merrill Lynch USD LIBID 6-Month Constant Maturity Index. The Short Duration portfolio is benchmarked against the Barclays Capital Treasury 1-3 Year Index. Over the course of investment operations to date, WTC Captive and its investment manager have found it possible to achieve the Company's investment objectives within this original two-portfolio structure, moving funds between the Liquidity and Short Duration portfolios and adjusting duration as appropriate. Notwithstanding, the Company, its investment manager, and the Board of Directors review the investment policy and portfolio structure from time to time to ensure that it continues to be responsive to the Company's needs and objectives. Such reviews have considered whether new portfolio asset classes should be introduced, and whether existing target asset allocation ranges continue to be appropriate, among other questions.

**WTC Captive Insurance Company, Inc.**  
**Management's Discussion and Analysis**

2013 saw the continued trend in recent years of lower levels of investment income commensurate with the investment rates for short maturity fixed income investments and the Company's reduced balances of investment assets, and in line with the Company's expectations. Gross investment income for the year ended December 31, 2013 totaled \$1.1 million compared to investment income of \$3.5 million for the year ended December 31, 2012. The lower level of investment income year over year is attributable to several factors. First, interest rates for short maturity fixed income investments continue to be extremely low by historical standards. To illustrate how these rates have impacted our portfolio, the market yield on our aggregate portfolio was 0.56% on January 1, 2013, while it had declined to under 0.20% by December 31, 2013. Second, the expected and continued decline in Company assets leaves fewer assets available upon which to earn a return. And finally, given the pendency of the reinsurance transaction described above, funds within the "Short Duration" portfolio were liquidated to accommodate payment of the reinsurance transaction premium. These funds remain in a money market fund pending disposition of the transaction.

The following is a summary of WTC Captive's unrestricted investment securities, at fair value, as of December 31, 2013, 2012 and 2011:

<i>(Dollars in thousands)</i>	<u><b>2013</b></u>	<u><b>2012</b></u>	<u><b>2011</b></u>
Commercial paper	\$ -	\$ 5,839	\$ 8,187
U.S. govt. and agency securities	25,706	205,939	192,983
Corporate and other securities	7,704	79,862	80,713
State and municipal securities	3,400	10,321	30,064
Mortgage and asset backed securities	<u>-</u>	<u>43,326</u>	<u>57,703</u>
Total	<u><u>\$ 36,810</u></u>	<u><u>\$ 345,287</u></u>	<u><u>\$ 369,650</u></u>

In aggregate, these investments had an average Standard & Poor's (S&P) credit rating of "AA" and an effective duration of 0.35 years as of December 31, 2013. As of December 31, 2013, included among the U.S. government and agency securities, in the table above, are securities issued by Fannie Mae, Freddie Mac, the Federal Home Loan Bank and the Federal Home Loan Mortgage Corporation that do not carry the full faith and credit guarantee of the United States Government.

The following is a summary of WTC Captive's restricted investment securities, at fair value, as of December 31, 2013, 2012 and 2011:

<i>(Dollars in thousands)</i>	<u><b>2013</b></u>	<u><b>2012</b></u>	<u><b>2011</b></u>
Commercial paper	\$ -	\$ -	\$ -
U.S. govt. and agency securities	-	-	-
Corporate securities and other	-	-	-
State and municipal securities	<u>-</u>	<u>-</u>	<u>500</u>
Total	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 500</u></u>

*Deposit Accounting*

For reasons described below, the Contract between WTC Captive, the City and the Additional Named Insureds did not transfer "insurance risk" to the Company, as that term is defined in applicable accounting guidance.

## **WTC Captive Insurance Company, Inc.**

### **Management's Discussion and Analysis**

Accordingly, the transfer of funds to the Company was accounted for using "deposit accounting." Deposit accounting is applied when no insurance risk is present in a contract. When considered in its entirety, the Contract contains neither underwriting risk nor timing risk, two elements fundamental to the transfer of insurance risk.

Under deposit accounting, which focuses primarily on the Statements of Net Position, all financial activity related to the Contract is recorded through a "deposit liability" on the *Statements of Net Position*. The deposit liability represents the accrual for loss and loss adjustment expenses to be paid under the Contract. This liability is increased to the extent funds are received subject to the terms of the Contract, less the \$100 million originally designated to meet capital and surplus requirements held as a residual liability. Notwithstanding, the designation of funds to satisfy capital and surplus requirements does not restrict the ability of the Company to use such funds to satisfy its obligations.

Given the establishment of the deposit liability, no further recognition of loss or loss adjustment expense occurs. The deposit liability is reduced to the extent that loss and loss adjustment expenses are paid. Payment of such expenses does not impact the *Statements of Activities*. The deposit liability is adjusted upward for "interest accretion" at each reporting date. Interest accretion enables the Company to recognize additional liability that will be recorded by the Company over the period of its estimated life (pursuant to the Contract) in excess of the original deposit amount. The deposit liability is accreted based on the Contract's internal rate of return ("IRR"). The IRR is the estimated rate required to discount amounts that will be paid under the Contract back to the original deposit amount. The accretion of the deposit liability is designed to match interest expense against related investment income attributable to the deposit liability, thereby limiting recognition of income derived from the Contract. This treatment is appropriate given the nature of the economic relationship, as described above.

As a result of a review conducted by the Company and certain of its service providers in 2011, the Company changed to an IRR of 2.5%. The Company used this rate in its financial calculations for the year ended December 31, 2011, and made appropriate historical adjustments for 2004 through 2010, as required under its accounting model. The Company continued to use an IRR of 2.5% for 2012 and 2013 based on reviews conducted by the Company and certain of its service providers in 2012 and 2013, respectively. It is expected that the IRR will be less than the expected return on invested assets due to the cost of operating the Company that impacts the Contract limits (i.e., operating expenses are not payments under the Contract). Additionally, interest accretion is calculated only on the deposit liability, while investment yield is derived from all invested assets. The IRR is subject to significant uncertainty due to changes in the timing and amount of future cash flows, the cyclicity of general economic conditions, and fluctuations in the rate of return achieved with respect to the investment portfolio. The IRR estimate of 2.5% at December 31, 2013 was based on a number of scenarios developed at investment rates of return ranging from 1.28% to 3.39%, given varying payout patterns, settlement structures, and other factors. The IRR estimate of 2.5% at December 31, 2012 was based on a number of scenarios developed at investment rates of return ranging from 0.75% to 3.25%, given varying payout patterns, settlement structures, and other factors. The IRR estimate of 2.5% at December 31, 2011 was based on a number of scenarios developed at investment rates of return ranging from 1.00% to 3.50%, given varying payout patterns, settlement structures, and other factors. The increase in the IRR from 2.0% to 2.5% in 2011 was primarily a result of more heavily weighting payment scenarios that approximate the terms of the Amended SPA and interest rates achieved or expected from inception through 2012 (when the final payments were expected on the settlement liability).

An interest rate accretion expense of \$5.1 million was recognized for the year ended December 31, 2013. An interest rate accretion expense of \$6.0 million was recognized for the year ended December 31, 2012. An interest accretion expense of \$6.9 million, together with an interest accretion expense rate adjustment of \$27.3 million, was recognized for the year ended December 31, 2011.

**WTC Captive Insurance Company, Inc.**  
**Management's Discussion and Analysis**

As noted above, under deposit accounting all activity related to the Contract is recorded through the deposit liability. Payment of such expenses does not impact the *Statements of Activities*. Activity within the deposit liability, including interest accretion and payments made from the deposit for the years ended December 31, 2013, 2012 and 2011, respectively, are summarized in the table below:

<i>(Dollars in thousands)</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Liability at beginning of year	\$ 213,887	\$ 257,313	\$ 263,846
Interest accretion	5,063	5,982	34,185
Transfer to debris removal liability account	(3,800)	-	-
LAE - adjusting paid	(6,744)	(1,457)	(3,039)
LAE - all other paid	(1,518)	(28,787)	(25,129)
Indemnity payments	(9,080)	(19,164)	(50)
Debris removal settlement liability transfer	-	-	(12,500)
	<u>          </u>	<u>          </u>	<u>          </u>
Liability at end of year	<u>\$ 197,808</u>	<u>\$ 213,887</u>	<u>\$ 257,313</u>

*Loss Reserves and Estimated Ultimate Losses*

Management of WTC Captive has engaged an independent actuarial consulting firm to provide an assessment of the timing of payments to be made pursuant to the Contract, to provide support in calculating the interest accretion expense described above and to provide a projection of ultimate loss when more meaningful information becomes available. The ultimate liability for loss and loss adjustment expenses has not been estimated as of December 31, 2013, 2012 and 2011.

No estimate for losses incurred but not reported ("IBNR") has been developed to date. There would be no differences to the deposit liability recorded by the Company or other related balances had an actuarial study been completed with respect to December 31, 2013, 2012 and 2011, because of the use of deposit accounting discussed above. Any future estimate of ultimate loss and loss adjustment expenses may be uncertain due to limited historical reference data, uncertainty related to potential judicial decisions, the developing science surrounding the alleged injuries, the latent manifestation periods that may apply to such alleged injuries, changes in interest rates, general economic conditions and other uncertainties.

From 2005 through 2010, WTC Captive set case reserves based on a methodology it developed in 2005. The Company's considerations in establishing this methodology were to: i) count and track the number of individual plaintiffs, as opposed to individual claims (defined as individual plaintiffs suing multiple insureds), ii) recognize that, at the then early stage of the litigation, the Company would not have sufficient information upon which to establish meaningful reserves for individual cases, and iii) set an initial reserve for loss adjustment expenses generally of \$10,000 and a \$1,000 reserve for the loss itself as a "placeholder." Given the Amended SPA and the separation of over \$625 million in restricted funds established to fulfill the Company's obligation under the settlement, WTC Captive modified this procedure. In 2011, the Company recognized that reserves for the settlement participants consisted of the restricted assets separated pursuant to the Amended SPA, while we established placeholder reserves in the amounts indicated above for those open claims not a part of the debris removal settlement. In 2013, WTC Captive modified this methodology once more by establishing actual reserves on all remaining open claims, while continuing to recognize the restricted assets as our reserves for the settlement participants under the Amended SPA. Under this methodology, reserves totaled \$4.9 million as of December 31, 2013. Finally, it is important to recognize that given the structure and terms of both the Contract and the Company's organizational documents, together with the Company's use of deposit accounting, case reserves do not carry the importance that they do for typical insurance company operations.

**WTC Captive Insurance Company, Inc.**  
**Management's Discussion and Analysis**

Of note in this regard, case reserves are not reflected in any of the Company's basic financial statements. Furthermore, case reserves do not necessarily provide any indication as to the resources of the Company available to satisfy claims covered under the Contract. Ultimately, the entirety of the financial resources of the Company is available to meet the Company's obligations under the Contract.

*Statements of Activities*

The following is a summary of WTC Captive's *Statements of Activities* for the years ended December 31, 2013, December 31, 2012 and December 31, 2011:

<i>(Dollars in thousands )</i>	<u><b>2013</b></u>	<u><b>2012</b></u>	<u><b>2011</b></u>
<b>Investment income and operating revenue</b>			
Investment income before interest accretion	\$ 1,121	\$ 3,487	\$ 6,266
Interest accretion on deposit liability	<u>(5,063)</u>	<u>(5,982)</u>	<u>(34,185)</u>
Net investment loss and operating revenue	(3,942)	(2,495)	(27,919)
<b>Operating expenses</b>			
Professional and management fees	2,987	3,082	3,643
Personnel expenses	996	972	959
General and administrative expenses	<u>521</u>	<u>589</u>	<u>573</u>
Total operating expenses	<u>4,504</u>	<u>4,643</u>	<u>5,175</u>
Net operating loss	<u><u>\$ (8,446)</u></u>	<u><u>\$ (7,138)</u></u>	<u><u>\$ (33,094)</u></u>

*Investment Income*

Investment income consists of interest earned on the Company's money market account and investment portfolio and realized and unrealized gains (losses) on the Company's marketable securities. Investment income totaled \$1.1 million, \$3.5 million and \$6.3 million for the years ended December 31, 2013, 2012 and 2011 respectively. These investment returns are gross of accretion expense, and equate to annualized returns of approximately 0.3%, 0.9% and 1.5%, for the years ended December 31, 2013, 2012 and 2011 respectively.

Investment income on the Company's restricted cash and investments consists of interest earned and realized and unrealized gains (losses) on marketable securities in the debris removal settlement portfolio. Investment income on restricted cash and investments does not flow through the Company's Statements of Activities. Investment income credited to the debris removal settlement fund totaled \$372, \$5,000 and \$1.1 million for the years ended December 31, 2013, 2012 and 2011 respectively.

As shown in the table above, interest accretion is netted against gross investment income to yield net investment income. As discussed under Deposit Accounting, the rate used to calculate interest accretion was changed in 2011 from 2.0% to 2.5%. The \$5.1 million in interest accretion expense for 2013 includes interest accretion on the deposit liability at 2.5%. The \$6.0 million in interest accretion expense for 2012 includes interest accretion on the deposit liability at 2.5%. The \$34.2 million in interest accretion expense for 2011 includes \$6.9 million in interest accretion expense on the deposit liability at 2.5% for 2011, as well as a \$27.3 million life to date interest accretion expense adjustment for previous years to bring accretion expense for those years from their original amounts to the new rate of 2.5%.

**WTC Captive Insurance Company, Inc.  
Management's Discussion and Analysis**

*Professional and Management Fees*

Professional and management fees include the expenses of third party service providers that assist in the general operation of the Company. For example, the expenses of the Company's auditor, actuary, captive manager, and corporate counsel, among others, are included in this category.

*Personnel Expenses*

Personnel expenses include the salaries, benefits and payroll taxes for the Company's employees.

*General and Administrative Expenses*

General and administrative expenses include other costs of operating the Company. Insurance, rent, office supplies, computer and telecommunications expenses are included in this category.

*For Further Information*

This financial report is designed to provide a general overview of WTC Captive's finances for various stakeholders of the Company. Questions concerning any of the information provided in this report should be addressed to WTC Captive Insurance Company, Inc., 100 William Street, Suite 2001, New York, NY 10038.

**WTC Captive Insurance Company, Inc.**  
**Statements of Net Position**  
**December 31, 2013 and 2012**  
*(In Thousands)*

	<u>2013</u>	<u>2012</u>
<b>Assets</b>		
Cash and cash equivalents	\$ 290,914	\$ 6,272
Cash and cash equivalents - restricted	<u>4,077</u>	<u>4,608</u>
Total cash and cash equivalents	<b>294,991</b>	10,880
Investments, at fair value	<b>36,810</b>	345,287
Accrued investment income	<b>82</b>	938
Prepaid expenses	<b>34</b>	33
Other assets	<u>5</u>	<u>5</u>
Total assets	<u><b>\$ 331,922</b></u>	<u><b>\$ 357,143</b></u>
<b>Liabilities</b>		
Debris removal settlement liability	\$ 4,077	\$ 4,608
Accrued expenses	<b>105</b>	270
Non-current liabilities:		
Deposit liability	<b>197,808</b>	213,887
Residual liability	<u><b>129,932</b></u>	<u>138,378</u>
Total liabilities	<u><b>\$ 331,922</b></u>	<u><b>\$ 357,143</b></u>

The accompanying notes are an integral part of these financial statements.



**WTC Captive Insurance Company, Inc.**  
**Statements of Activities**  
**For the Years Ended December 31, 2013 and 2012**  
*(In Thousands)*

	<u>2013</u>	<u>2012</u>
Investment income and operating revenues (losses):		
Investment income before interest accretion	\$ 1,121	\$ 3,487
Interest accretion expense on deposit liability	<u>(5,063)</u>	<u>(5,982)</u>
Net investment income and operating revenues (losses)	(3,942)	(2,495)
Operating expenses:		
Professional and management fees	2,987	3,082
Personnel expenses	996	972
General and administrative expenses	<u>521</u>	<u>589</u>
Total operating expenses	4,504	4,643
Net operating loss	(8,446)	(7,138)
Residual liability, beginning of year	<u>138,378</u>	<u>145,516</u>
Residual liability, end of year	<u><u>\$ 129,932</u></u>	<u><u>\$ 138,378</u></u>

The accompanying notes are an integral part of these financial statements.

**WTC Captive Insurance Company, Inc.**  
**Statements of Cash Flows**  
**For the Years Ended December 31, 2013 and 2012**  
*(In Thousands)*

	<u>2013</u>	<u>2012</u>
Cash flows from operating activities:		
Cash paid for employee salaries and benefits	\$ (996)	\$ (972)
Losses and loss adjustment expenses paid	(21,674)	(427,718)
Professional and management fees paid	(3,249)	(3,365)
General and administrative expenses paid	(521)	(589)
Interest income collected	4,893	3,546
Interest income collected - restricted funds	-	5
	<u>(21,547)</u>	<u>(429,093)</u>
Net cash flows from operating activities	(21,547)	(429,093)
Cash flows from investing activities:		
Purchase of investments	(348,838)	(810,314)
Sales and maturities of investments	654,496	833,321
	<u>305,658</u>	<u>23,007</u>
Net cash flows from investment activities	305,658	23,007
Increase (decrease) in cash and cash equivalents	284,111	(406,086)
Cash and cash equivalents, beginning of year	10,880	416,966
Cash and cash equivalents, end of year	<u>\$ 294,991</u>	<u>\$ 10,880</u>
Reconciliation of net operating loss to net cash flows from operating activities:		
Net operating loss	\$ (8,446)	\$ (7,138)
Adjustments to reconcile net operating loss to net cash used in operating activities:		
Realized losses (gains) on sales of investments	3,159	(261)
Unrealized (gains) losses on investments	(340)	2,117
Changes in operating assets and liabilities:		
Accrued investment income	856	84
Prepaid expenses and other assets	(1)	-
Debris removal settlement liability	(531)	(380,185)
Accrued expenses	(165)	(284)
Deposit liability	(16,079)	(43,426)
Net cash from operating activities	<u>\$ (21,547)</u>	<u>\$ (429,093)</u>

The accompanying notes are an integral part of these financial statements.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 1 - Organization**

WTC Captive Insurance Company, Inc. (“WTC Captive” or the “Company”) is a not-for-profit corporation formed in the State of New York in response to the events of September 11, 2001. WTC Captive was established pursuant to the Consolidated Appropriations Resolution, 2003, P.L. 108-7, signed by President Bush on February 20, 2003, and corollary enabling State of New York legislation. WTC Captive was incorporated on July 1, 2004; it was funded by the Federal Emergency Management Agency (“FEMA”), licensed as a captive insurance company by the New York State Department of Financial Services (“NYSDFS”) and commenced operations on December 3, 2004.

Pursuant to a liability insurance contract, WTC Captive provides specified coverage against certain third-party claims made against New York City (the “City”) and approximately 145 contractors and subcontractors (collectively, “Additional Named Insureds”) working on the City’s FEMA-funded debris removal project. WTC Captive coverage includes general liability, environmental liability, professional liability and marine liability. Coverage is provided on both an excess of loss and first dollar basis, depending on the line of coverage.

WTC Captive employs a President who also serves as Chief Executive Officer. Additionally, a Treasurer/Chief Financial Officer and General Counsel/Secretary are employed by the Company. WTC Captive engages several independent service providers, under the direction of the President/CEO, Officers and the Board of Directors, to carry out various functions of the Company. Such services include third party administrative claims management, accounting, regulatory compliance, investment management, actuarial consulting, corporate legal and claims/defense counsel, among others.

WTC Captive was funded on December 3, 2004 with \$999.9 million in funds. These funds originated from FEMA pursuant to the Consolidated Appropriations Resolution, 2003, P.L. 108-7. FEMA disbursed these funds to the State of New York pursuant to a grant agreement (“FEMA Grant Agreement”) between FEMA and the New York State Department of Homeland Security and Emergency Services (“DHSES”). DHSES then transferred the funds to the City pursuant to a sub-grant agreement (“DHSES Sub-Grant Agreement”). Finally, the City transferred the funding to WTC Captive pursuant to an agreement (the “City/Captive Agreement”). WTC Captive used this funding to support issuance of an insurance contract (the “Contract”), the policyholders of which are the City and the Additional Named Insureds, as more fully described in Notes 2 and 5.

Funds amounting to \$899.9 million were recorded directly to “deposit liability,” on the *Statements of Net Position*, as more fully described below. The Company’s Board of Directors approved the designation of \$100 million to satisfy the capital and surplus requirements of the NYSDFS, as required by Section 7004 of the New York Insurance Law, Article 70. The designation of \$100 million was based on an assessment of factors that would impact amounts designated as capital, primarily related to potential changes in the market value of the investment portfolio, which are charged directly to operations, and the potential for interest accretion and general and administrative expenses to exceed gross investment income in a given year, as more fully described below. WTC Captive holds the amounts designated to satisfy capital and surplus as a liability, “residual liability” on its *Statements of Net Position*. Amounts designated to satisfy capital and surplus requirements are held as a liability, rather than as residual net assets, due to provisions of the Company’s organizational documents that require the Company to return funding that remains, if any, after all obligations have been satisfied, as defined by and according to the terms of the organizational documents. Additionally, any net gain or loss from operations will directly impact the Company’s residual liability designated to satisfy capital and surplus requirements. As such, the net loss recorded for the years ended December 31, 2013 and 2012, respectively, have been reflected within the residual liability on the Company’s *Statements of Net Position*. Designation of funds to satisfy capital and surplus requirements does not restrict the ability of the Company to use such funds to satisfy its obligations, as more fully described in Note 5.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 2 - Summary of Significant Accounting Policies**

**Basis of Accounting** - The financial statements of WTC Captive have been prepared using the accrual basis of accounting in conformity with accounting principles generally accepted in the United States ("GAAP"), as applied to governmental entities. WTC Captive is subject to accounting standards promulgated by the Governmental Accounting Standards Board ("GASB"), as applied by the City. GASB is recognized as the accepted standard-setting body for the promulgation of accounting and financial reporting principles applicable to U.S. state and local governmental entities. WTC Captive is included as a component unit of the City for financial reporting purposes.

WTC Captive entered into the Settlement Process Agreement, as Amended ("Amended SPA") in June 2010, which includes a base settlement amount of \$625 million. These funds were placed into a separately managed account, still under WTC Captive's control, in early September 2010. As a result of the Amended SPA and the segregation of these funds, certain cash and invested asset disclosures shown herein are indicated as unrestricted or restricted.

**Cash and Cash Equivalents** - WTC Captive considers all cash and highly liquid instruments with original maturities of three months or less to be cash equivalents. This includes cash, money market accounts and short-term commercial paper. Cash and cash equivalents held at December 31, 2013 and 2012 were as follows:

<i>(In thousands)</i>	<b>2013</b>	<b>2012</b>
Cash and Cash Equivalents:		
Cash - checking account	\$ 44	\$ 44
Cash - money market funds	278,970	4,228
Government agency discount notes	9,500	-
Commercial paper	2,400	2,000
Total	<b>290,914</b>	6,272
Cash and Cash Equivalents - Restricted:		
Cash - money market funds	4,077	4,608
Total cash and cash equivalents	<b>\$ 294,991</b>	<b>\$ 10,880</b>

**Investments** - Investments are recorded in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* ("Statement No. 31"). Statement No. 31 establishes fair value standards on accounting for all investments held by governmental entities. All investment income, including changes in the market value of investments, is recognized in the *Statements of Activities*. Realized gains and losses on the sale of investments are recognized on the specific identification basis to determine the costs of the investments sold.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 2 - Summary of Significant Accounting Policies (continued)**

Investments held by WTC Captive as of December 31, 2013 included U.S. Government and Agency securities, corporate debt securities and issues of state and local governments. Investments held by WTC Captive as of December 31, 2012 included commercial paper, U.S. Government and Agency securities, corporate debt securities, issues of state and local governments, mortgage-backed securities and asset-backed securities. The calculation of realized gains and losses is with respect to securities sold in the current year. This calculation is independent of the calculation of the change in the unrealized gains or losses of investments. Realized gains and losses on investments that are held in more than one year and sold in the current year are included as a change in the unrealized gains or losses of investments reported in the prior year(s). Investments are stated at fair value based on quoted market prices.

**Use of Estimates and Assumptions** - The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could materially impact the amounts reported and disclosed herein.

**Deposit Accounting** - As more fully described in Note 5, the Contract between WTC Captive, the City and the Additional Named Insureds did not transfer “insurance risk” to the Company, as that term is defined in applicable accounting guidance. Accordingly, the transfer of funds to the Company was accounted for using “deposit accounting.” Deposit accounting is applied when no insurance risk is present in a contract. When considered in its entirety, the Contract contains neither underwriting risk nor timing risk, two elements fundamental to the transfer of insurance risk.

Under deposit accounting, which focuses primarily on the balance sheet, all financial activity related to the Contract is recorded through a “deposit liability” on the *Statements of Net Position*. The deposit liability represents the accrual for loss and loss adjustment expenses to be paid under the Contract. This liability is increased to the extent funds are received subject to the terms of the Contract, less the \$100 million originally designated to meet capital and surplus requirements held as a residual liability. Notwithstanding, the designation of funds to satisfy capital and surplus requirements does not restrict the ability of the Company to use such funds to satisfy its obligations. Given the establishment of the deposit liability, no further recognition of loss or loss adjustment expenses occurs. The deposit liability is reduced to the extent that loss and loss adjustment expenses are paid. Payment of such expenses does not impact the *Statements of Activities*. The deposit liability is adjusted upward for “interest accretion” at each reporting date. Interest accretion enables the Company to recognize additional liability that will be recorded by the Company over the period of its estimated life (pursuant to the Contract) in excess of the original deposit amount. The deposit liability is accreted based on the Contract’s internal rate of return (“IRR”). The IRR is the estimated rate required to discount amounts that will be paid under the Contract back to the original deposit amount. The accretion of the deposit liability is designed to match interest expense against related investment income attributable to the deposit liability, thereby limiting recognition of income derived from the Contract. This is appropriate given the nature of the economic relationship, as described above.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 2 - Summary of Significant Accounting Policies (continued)**

As a result of a review conducted by the Company and certain of its service providers in 2011, the Company changed to an IRR of 2.5%. The Company used this rate in its financial calculations for the year ended December 31, 2011, and made appropriate historical adjustments for 2004 through 2010, as required under its accounting model. The Company continued to use an IRR of 2.5% for 2012 and 2013 based on reviews conducted by the Company and certain of its service providers in 2012 and 2013, respectively. It is expected that the IRR will be less than the expected return on invested assets due to the cost of operating the Company that will impact the Contract limits (i.e., operating expenses are not payments under the Contract). Additionally, interest accretion is calculated only on the deposit liability, while investment yield is derived from all invested assets. The IRR is subject to significant uncertainty due to changes in the timing and amount of future cash flows, the cyclicity of general economic conditions, and fluctuations in the rate of return achieved with respect to the investment portfolio. The IRR estimate of 2.5% at December 31, 2013 was based on a number of scenarios developed at investment rates of return ranging from 1.28% to 3.39%, given varying payout patterns, settlement structures, and other factors. The IRR estimate of 2.5% at December 31, 2012 was based on a number of scenarios developed at investment rates of return ranging from 0.75% to 3.25%, given varying payout patterns, settlement structures, and other factors.

An interest rate accretion expense of \$5.1 million was recognized for the year ended December 31, 2013. An interest rate accretion expense of \$6.0 million was recognized for the year ended December 31, 2012. Interest accretion expense is presented as a component of net investment income as detailed in Note 3. Activity within the deposit liability, including interest accretion and payments made from the deposit, is detailed in Note 5.

Management of WTC Captive has engaged an independent actuarial consulting firm to provide an assessment of timing of payments to be made pursuant to the Contract, to provide support in calculating the interest accretion expense described above and to provide a projection of ultimate loss when more meaningful information becomes available. No estimate for losses incurred but not reported ("IBNR") has been developed to date. There would be no difference to the deposit liability recorded by the Company or other related balances had an actuarial study been completed at December 31, 2013 and 2012, because of the use of deposit accounting as discussed above.

**Taxes** - WTC Captive has been exempted from Federal tax pursuant to section 501(c)(4) of the Internal Revenue Code and from filing any annual or other information returns. Additionally, by statute, the Company is not subject to any New York State or local taxes or fees.

**Employee Benefits** - WTC Captive offers medical, dental, short-term and long-term disability, life insurance and a 401(k) defined contribution plan to all employees. Contributions to the 401(k) plan by WTC Captive were \$27,051 and \$21,980, for the years ended December 31, 2013 and 2012, respectively, and are included within personnel expenses on the Statements of Activities. The Company does not offer any other post-employment benefits.

**Subsequent Events** - WTC Captive has evaluated subsequent events for disclosure and recognition through March 10, 2014, the date the financial statements were available to be issued. Other than Note 7 and 8, management believes there are no subsequent events having an impact on the financial statements.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 2 - Summary of Significant Accounting Policies (continued)**

**Recent accounting standards** - In 2012, the WTC Captive adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and American Institute of Certified Public Accountants (AICPA) Pronouncements* (GASB No. 62). This standard improves financial reporting by incorporating into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the Financial Accounting Standards Board (FASB) and the AICPA pronouncements issued on or before November 30, 1989, which does not conflict or contradict GASB pronouncements. GASB No. 62 superseded GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*. The adoption of this new standard did not have a significant impact on the WTC Captive.

In June 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. The objective of this standard is to provide guidance for reporting deferred outflows of resources, deferred inflows of resources and net position in a statement of net position. Amounts that are required to be reported as deferred outflows should be reported in a statement of net position in a separate section following assets. Similarly, amounts to be reported as deferred inflows of resources should be reported in a separate section following liabilities. The statement of net position should report the residual amount as net position, rather than net assets. The provisions of this standard are effective for financial statements for periods beginning after December 15, 2011. The adoption of this new standard did not have a significant impact on the WTC Captive.

In 2013, the WTC Captive adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* (GASB No. 65). This standard improves financial reporting by clarifying the appropriate use of the financial statement elements deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The adoption of this new standard did not have a significant impact on the WTC Captive.

**Note 3 - Investments**

The amortized cost and fair value of unrestricted investments in debt securities, as of December 31, 2013, are as follows:

<i>(In thousands)</i>	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
U.S. government and agency securities	\$ 25,708	\$ -	\$ (2)	\$ 25,706
Corporate and other securities	7,733	-	(29)	7,704
State and municipal securities	<u>3,400</u>	<u>-</u>	<u>-</u>	<u>3,400</u>
Total	<u>\$ 36,841</u>	<u>\$ -</u>	<u>\$ (31)</u>	<u>\$ 36,810</u>

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 3 - Investments (continued)**

The amortized cost and fair value of unrestricted investments in debt securities as of December 31, 2012, are as follows:

<i>(In thousands )</i>	<u><b>Amortized Cost</b></u>	<u><b>Unrealized Gains</b></u>	<u><b>Unrealized Losses</b></u>	<u><b>Fair Value</b></u>
Commercial paper	\$ 5,839	\$ -	\$ -	\$ 5,839
U.S. government and agency securities	205,892	188	(141)	205,939
Corporate and other securities	80,467	457	(1,062)	79,862
State and municipal securities	10,285	36	-	10,321
Mortgage and asset-backed securities	43,175	450	(299)	43,326
Total	<u>\$ 345,658</u>	<u>\$ 1,131</u>	<u>\$ (1,502)</u>	<u>\$ 345,287</u>

The amortized cost and fair value of investments held as of December 31, 2013, by expected maturities, are shown below. Actual maturities may vary from expected maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

<i>(In thousands )</i>	<u><b>Amortized Cost</b></u>	<u><b>Fair Value</b></u>
Due in one year or less	\$ 33,441	\$ 33,410
Due after one year through five years	-	-
Due after five years through ten years	-	-
Due after ten years through twenty years	-	-
Due after twenty years	3,400	3,400
Total	<u>\$ 36,841</u>	<u>\$ 36,810</u>

WTC Captive's Board of Directors' approved investment policy statement outlines the Company's investment objectives, policies and procedures, among other matters. WTC Captive's broad investment objective emphasizes the preservation of invested assets and maintenance of sufficient liquidity to meet the Company's obligations, as defined by the Contract. As a secondary objective, the Company's investment policy seeks to achieve a total return that exceeds, after management fees, the benchmarks approved by the Board of Directors.



**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 3 - Investments (continued)**

The table below summarizes the average Standard & Poor's ("S&P") credit rating and effective duration by investment type, as of December 31, 2013:

<i>(In thousands )</i>	<u>Fair Value</u>	<u>S&amp;P Rating</u>	<u>Effective Duration</u>
U.S. government and agency securities	\$ 25,706	AA	0.44
Corporate and other securities	7,704	AA-	0.19
State and municipal securities	<u>3,400</u>	A	0.00
Total	<u><u>\$ 36,810</u></u>		

Included among the U.S. government and agency securities, in the table above, are securities issued by Fannie Mae, Freddie Mac, the Federal Home Loan Bank and the Federal Home Loan Mortgage Corporation that do not carry the full faith and credit guarantee of the United States Government. As of December 31, 2013, the Company did not hold any investments in mortgage and asset-backed securities. As of December 31, 2013, these investments, in aggregate, had an average S&P credit rating of "AA" and an effective duration of 0.35 years.

Effective duration is a measure of the price volatility of fixed-maturity investments to changes in interest rates, expressed in years and calculated as the time-weighted present value of future cash flows. The calculation of effective duration makes assumptions regarding the most likely timing and amounts of variable cash flows for investments that are highly sensitive to interest rate changes, such as mortgage-backed securities and callable bonds.

Gross realized gains on sales of investments amounted to \$1.3 million and \$2.8 million for the years ended December 31, 2013 and 2012, respectively. Gross realized losses on sales of investments amounted to \$4.5 million and \$2.5 million for the years ended December 31, 2013 and 2012, respectively. Realized gains and losses on sales of investments are included as a component of investment income before interest accretion on the *Statements of Activities*.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 3 - Investments (continued)**

Investment income recorded for the years ended December 31, 2013 and 2012, is detailed as follows:

<i>(In thousands)</i>	<u><b>2013</b></u>	<u><b>2012</b></u>
Interest income	\$ <b>4,353</b>	\$ 5,956
Net realized (losses) gains on sales of investments	<b>(3,159)</b>	261
Change in unrealized losses on investments	<b>340</b>	(2,117)
Investment management fees	<u><b>(413)</b></u>	<u>(613)</u>
Investment income before accretion expense	<b>1,121</b>	3,487
Interest accretion expense	<u><b>(5,063)</b></u>	<u>(5,982)</u>
Total	<u><u><b>\$ (3,942)</b></u></u>	<u><u><b>\$ (2,495)</b></u></u>

**Fair Value Measurements** - WTC Captive has chosen to use the fair value measurements and disclosures based on the guidance promulgated by the FASB Accounting Standards Codification. This guidance defines fair value, establishes a framework and hierarchy for measuring fair value, and expands disclosures about fair value measurements.

WTC Captive estimates of fair value for financial assets and financial liabilities are based on the framework established in the fair value measurements and disclosures accounting guidance. The framework is based on the inputs used in valuation and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the fair value accounting guidance hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions.

The three levels of the hierarchy are as follows:

Level 1 - Inputs to the valuation methodology are quoted prices for identical assets or liabilities traded in active markets.

Level 2 - Inputs to the valuation methodology 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 and market corroborated inputs.

Level 3 - Inputs to the valuation methodology are unobservable for the asset or liability and are significant to the fair value measurement.

Fair values are based on quoted market prices when available (Level 1). When market prices are not available, fair value is generally estimated using current market inputs for similar financial instruments with comparable terms and credit quality, commonly referred to as matrix pricing (Level 2). All of the Company's investments as of December 31, 2013 and 2012 have been valued using pricing inputs consistent with Level 1 or Level 2 categorization.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 3 - Investments (continued)**

The following tables present the levels, within the fair value hierarchy, at which the Company's financial assets are measured on a recurring basis, as of December 31, 2013 and 2012:

December 31, 2013 (In thousands)	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
U.S. government and agency securities	\$ 9,498	\$ 16,208	\$ -	\$ 25,706
Corporate and other securities	-	7,704	-	7,704
State and municipal securities	-	3,400	-	3,400
Total	<u>\$ 9,498</u>	<u>\$ 27,312</u>	<u>\$ -</u>	<u>\$ 36,810</u>
December 31, 2012 (In thousands)	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Commercial paper	\$ -	\$ 5,839	\$ -	\$ 5,839
U.S. government and agency securities	168,245	37,694	-	205,939
Corporate and other securities	-	79,862	-	79,862
State and municipal securities	-	10,321	-	10,321
Mortgage and asset-backed securities	-	43,326	-	43,326
Total	<u>\$ 168,245</u>	<u>\$ 177,042</u>	<u>\$ -</u>	<u>\$ 345,287</u>

**Note 4 - Investments - Restricted**

In accordance with the Amended SPA, as more fully described in Notes 2 and 5, the Company transferred funds into a separate investment account during 2010. Although these funds were restricted in accordance with the Amended SPA, WTC Captive directed the investment allocation of the funds. At December 31, 2013 and 2012, respectively, there were no restricted investment securities held by the Company.

There were no realized gains or losses reported on restricted investments as of December 31, 2012 since the last remaining restricted investment was redeemed in 2012 for \$500,000 with an amortized cost of \$500,000, resulting in \$0 realized gains or losses. There were no realized gains or losses reported on restricted investments as of December 31, 2013 as no restricted investment securities were held during the year. Realized gains and losses on sales of restricted investments are included as a component of the Debris Removal Settlement Liability, as reported on the *Statements of Net Position*.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 4 - Investments - Restricted (continued)**

**Investment Income** - Investment income recorded on restricted cash and investments for the years ended December 31, 2013 and 2012 was approximately \$372 and \$5,000, respectively.

**Note 5 - Insurance Activity**

Pursuant to a liability insurance contract (the “Contract”), WTC Captive provides a wide range of coverage against third-party claims made against the City and the Additional Named Insureds. WTC Captive coverage includes general liability, environmental liability, professional liability and marine liability. Coverage is provided on both an excess of loss and first dollar basis, depending on the line of coverage. The policy effective dates are from September 11, 2001 (post-collapse) through August 30, 2002. This period is referred to as the “exposure period.” This is the only insurance contract that has or will be issued by WTC Captive and all of the Company’s business activities relate to its obligations under the Contract.

The coverage limits contained in the Contract have been defined and are limited by an “experience account” that by design is expected to fluctuate with the Company’s resources. The experience account consists of funding received, plus investment returns, less loss and loss adjustment expenses and all costs associated with operating the Company. As such, these coverage limits are subject to significant uncertainty due to the amount and timing of future cash flows, investment returns achieved in the investment portfolio and other factors outside the Company’s control. The policy contains sub-limits applicable to certain classes of claims, which are subject to adjustment. Additionally, the policy contains “non-acceptance of claims” and “reduced claim payment” terms. These terms serve to limit the obligation of the Company once the experience account is reduced to predetermined levels as defined in the Contract.

On June 23, 2010, the Settlement Process Agreement, as Amended (the “Amended SPA”) was reached with attorneys representing over 10,000 plaintiffs and approved by Judge Hellerstein. The Amended SPA contained several financial components to be contributed by the WTC Captive: i) a base settlement contribution of \$625 million; ii) opt-in bonus payments of 2% of the settlement amount for every one percent in excess of the 95% opt-in requirement, and if the opt-in threshold exceeds 98%, additional opt-in bonus payments of one-fifth of one percent (0.20%) for every tenth of one percent (0.10%) above the 98% opt-in rate. At a 100% opt-in rate the bonus payments would total 10% of the settlement amount; iii) a contingent payment structure of up to \$25 million; iv) a contribution of \$3.5 million towards the costs of administering the settlement; and v) a contribution of the WTC Captive’s interest in an underlying marine insurance policy. In 2011 the parties signed a settlement agreement concerning this underlying marine policy and on June 9, 2011, \$28 million was transferred to the Amended SPA settlement account.

On January 5, 2011, the parties to the settlement signed the affirmation of final settlement, triggering the claims evaluation process and beginning the process of distributing payments. The first round of payments under the settlement was made on January 27, 2011. On March 4, 2011, WTC Captive determined that the opt-in percentage to the settlement exceeded 96%. This triggered a bonus payment of \$12.5 million that WTC Captive deposited into the settlement account on March 7, 2011.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 5 - Insurance Activity (continued)**

The WTC Captive's insureds have appealed a series of rulings and actions by Judge Alvin Hellerstein relative to the settlement, including his determination that the involuntary dismissal of plaintiffs should reduce the denominator for the opt-in calculations, which would result in greater opt-in "bonus" payments under the settlement. On September 8, 2011, Judge Hellerstein issued a final order concerning calculation of the settlement opt-in percentage, updating his December 30, 2010 order on the matter. The WTC Captive continues to disagree with the logic and calculation in this ruling. However, \$42.5 million has been placed in a separate account pending a ruling on the matter by the Second Circuit. In light of this separation of funds, the Company was able to obtain a stay of the September 8, 2011 order pending appeal.

The appeal on the opt-in percentage has been consolidated with an appeal regarding the first contingent payment. As part of the Amended SPA, the WTC Captive agreed to make payments of up to \$5 million per year for each of the first five years following the affirmation of final settlement dependent upon a number of factors, including the number of new claims filed and the cost of resolving those claims. The first date for review of those criteria was January 5, 2012. Upon advice of counsel, there was no payment due because the number of post-settlement claims exceeded the threshold for payment as set forth in the Amended SPA. However, Judge Hellerstein issued an order dated July 13, 2012 interpreting the contingent payment terms of the Amended SPA such that the first contingent payment of \$5 million, calculated based on the number of new claims filed each year, was to be paid notwithstanding previous agreement by the parties that no such payment was due. Judge Hellerstein also directed that plaintiffs' counsel should not receive any fee on the contingent payments. The WTC Captive continues to dispute the issue and has taken an appeal, and plaintiffs' counsel has appealed the ruling on fees. The amount in question was deposited into the separate account pending the results of the appeal and the order was stayed.

The issue returned in January 2013 when the second contingent payment was due. Based on calculations according to the WTC Captive's appellate position, \$3.8 million was due in 2013 out of the possible \$5 million in contingent payments under the Amended SPA. The parties reached agreement that the WTC Captive would pay the actual plaintiffs' portion of this \$3.8 million, or about \$2.85 million, according to the terms of the Amended SPA, setting aside the attorneys' fees and the remaining \$1.2 million to be addressed according to the results of the appeal. The agreement is without prejudice to either side's position in the appeal. As a result, \$3.8 million was placed into the settlement account on January 15, 2013. The \$2.85 million agreed to be due to individual plaintiffs was paid out on January 16, 2013 according to instructions from the Allocation Neutral, while fees of about \$950,000 subject to appeal remained in the settlement account. The remaining \$1.2 million of the \$5 million was placed into the separate account pending results of the appeal. In total, about \$48.7 million has been placed in a separate account relative to the bonus and contingent payment appeals. Briefing is complete on the consolidated appeals and oral argument was presented in April 2013. Corporate counsel argued on behalf of the WTC Captive and its insureds, and the questions focused on issues of contract interpretation. A ruling is expected in 2014.

In January 2014, the third contingent payment was due. Under the terms of the Amended SPA, the full \$5 million was owed. On February 3, 2014, WTC Captive paid the actual plaintiffs' portion of the \$5 million, or about \$3.8 million, according to the terms of the Amended SPA, setting aside the attorneys' fees of about \$1.2 million to be addressed according to the results of the appeal.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 5 - Insurance Activity (continued)**

Apart from the settlement described above, there were 100 cases naming at least one WTC Captive insured as a defendant, not including various cases in which the plaintiff has filed a notice of withdrawal seeking dismissal in favor of the re-opened Victim Compensation Fund (“VCF”). These cases were all in active discovery in 2012, and the WTC Captive sought to resolve them where possible at appropriate amounts. While plaintiffs’ counsel was very interested in pursuing settlement discussions, Judge Hellerstein’s ambitious discovery schedule put pressure on the parties. WTC Captive management maintained a steady pace throughout 2012 with regular meetings with plaintiffs’ counsel. Ninety-two cases were settled in principle in 2012, 87 of them including significant claims of respiratory injury, the other five were non-respiratory cases as noted below. Total settlement value for those 87 cases is approximately \$20 million. In 2013, the WTC Captive continued to pursue resolution of outstanding claims, by motion practice and settlement. Three claims were dismissed by Judge Hellerstein, either based on the statute of limitations or for failure to comply with discovery obligations and court orders. Five claims were settled in 2013, two alleging primarily respiratory injury and three non-respiratory cases. The 2013 respiratory settlements totaled just under \$1 million.

The WTC Captive inherited the defense of several orthopedic injury cases against various insureds as a result of its settlements with the Liberty and London GL carriers. During the course of 2011, the WTC Captive awaited the deadline for the re-opened VCF to see what plaintiffs would remain rather than actively pursuing settlements. The WTC Captive settled five of these non-respiratory cases in principle, including one through mediation, during 2012. The total settlement value of these five cases is \$1.2 million. As noted above, three additional non-respiratory cases were settled in 2013, each of these went through mediation. The total value of the 2013 non-respiratory settlements was \$6.8 million.

The total value of 2013 settlements was \$7.7 million. Several claims settled in principle in 2012 were finalized and paid in 2013, and with a previous settlement in principle paid in January 2014 there are no incomplete settlements. Total settlement cost for the claims resolved in 2012 and 2013 was \$29 million, of which \$21 million was for respiratory cases and the remaining \$8 million was for non-respiratory cases. One new case was filed in 2012, but has not been in active discovery and remains open.

Under the terms of its Bylaws, grant agreements and the Contract, the WTC Captive is authorized, and at certain times required, to evaluate the purchase of assumption reinsurance. Assumption reinsurance would provide the Company the ability to reinsure some or all of its obligations. With the resolution of essentially all claims against the Company’s insureds, together with the reopening of the VCF, WTC Captive undertook its first such evaluation in 2013. Through the summer, WTC Captive undertook a competitive process to secure assumption reinsurance proposals. A Request for Proposal was developed, and eight global insurers were invited to compete for the opportunity. Two proposals were received, with one of the proposals offering terms most closely aligned with the Company’s goals. These goals are straightforward: increased limits of financial protection for all insureds within a transaction structure that benefits all insureds while harming none; comparable coverage terms to the existing Contract; true assumption reinsurance that assigns all rights and obligations of the WTC Captive under the Contract to the new insurer; a demonstrated understanding by the assuming insurer of the unique provisions of the Contract; and an insurer who can provide long-term financial security for the WTC Captive’s insureds. While the transaction was under regulatory review by NYSDFS and FEMA in November 2013, concerns raised by some members of Congress and by advocates for first responders put the transaction on hold. The transaction remains pending regulatory approval.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 5 - Insurance Activity (continued)**

Debris removal settlement liability activity related to the Amended SPA, for the years ended December 31, 2013 and 2012, is summarized in the table below:

<i>(In thousands)</i>	<u>2013</u>	<u>2012</u>
Liability at beginning of year	\$ 4,608	\$ 384,793
Investment income	-	5
Transfers in	3,800	-
Indemnity payments	<u>(4,331)</u>	<u>(380,190)</u>
Liability at end of year	<u>\$ 4,077</u>	<u>\$ 4,608</u>

Loss adjustment expenses (“LAE”) have been categorized into two groups. “LAE - adjusting” represents loss adjustment expenses related to claims adjusting and handling. “LAE - all other” includes all fees, costs and expenses allocable to any specific claim or claims that are incurred by the Company in the litigation, defense, appeal or settlement of a specific claim or claims. Deposit liability activity for the years ended December 31, 2013 and 2012, is summarized in the table below:

<i>(In thousands)</i>	<u>2013</u>	<u>2012</u>
Liability at beginning of year	\$ 213,887	\$ 257,313
Interest accretion	5,063	5,982
Transfer to debris removal liability account	(3,800)	-
LAE - adjusting paid	(6,744)	(1,457)
LAE - all other paid	(1,518)	(28,787)
Indemnity payments	<u>(9,080)</u>	<u>(19,164)</u>
Liability at end of year	<u>\$ 197,808</u>	<u>\$ 213,887</u>

**Note 6 - Regulatory Requirements**

WTC Captive was formed pursuant to New York Insurance Law, Article 70, Captive Insurance Companies. In accordance with this law, the New York State Department of Financial Services requires WTC Captive to submit its financial statements to the NYSDFS using the GAAP basis of accounting, with the exception of variances prescribed by New York State laws and regulations or as permitted by the NYSDFS. The laws of the State of New York require WTC Captive to maintain minimum policyholders’ surplus (net assets) of \$250,000. As described in Note 1, the Company has designated \$100 million to satisfy the capital and surplus requirements of the NYSDFS. Amounts designated to satisfy capital and surplus requirements are held as a liability, rather than as residual net assets, due to provisions of the Company’s organizational documents that require the Company to return any funding that remains, if any, after all obligations have been satisfied. Additionally, any net gain or loss from operations will directly impact the Company’s residual liability designated to satisfy capital and surplus requirements. WTC Captive’s residual liability, designated to satisfy capital and surplus requirements, amounted to \$129.9 million and \$138.4 million at December 31, 2013 and 2012, respectively.

**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 6 - Regulatory Requirements (continued)**

There are no differences between net assets and net loss as reported in these financial statements and the corresponding amounts reported in the 2013 and 2012 New York Captive Insurance Company Annual Statement.

**Note 7 - Contingencies**

On December 30, 2010 Judge Alvin Hellerstein issued orders directing that opt-in calculations for bonus payments under the Amended SPA reflect his dismissal of over 400 plaintiffs for failure to prosecute. On September 8, 2011, Judge Hellerstein issued a final order concerning calculation of the settlement opt-in percentage. The WTC Captive continues to disagree with the logic and calculation in this ruling. However, \$42.5 million has been placed in a separate account pending a ruling on the matter by the Second Circuit. In light of this separation of funds, the Company was able to obtain a stay of the September 8, 2011 order pending appeal.

The appeal on the opt-in percentage has been consolidated with an appeal regarding the first contingent payment. As part of the Amended SPA, the WTC Captive agreed to make payments of up to \$5 million per year for each of the first five years following the affirmation of final settlement dependent upon a number of factors, including the number of new claims filed and the cost of resolving those claims. The first date for review of those criteria was January 5, 2012. Upon advice of counsel, there was no payment due because the number of post-settlement claims exceeded the threshold for payment as set forth in the Amended SPA. However, Judge Hellerstein issued an order dated July 13, 2012 interpreting the contingent payment terms of the Amended SPA such that the first contingent payment of \$5 million, calculated based on the number of new claims filed each year, was to be paid notwithstanding previous agreement by the parties that no such payment was due. Judge Hellerstein also directed that plaintiffs' counsel should not receive any fee on the contingent payments. The WTC Captive continues to dispute the issue and has taken an appeal, and plaintiffs' counsel has appealed the ruling on fees. The amount in question was deposited into a separate account pending the results of the appeal and the order was stayed.

The issue returned in January 2013 when the second contingent payment was due. Based on calculations according to the WTC Captive's appellate position, \$3.8 million was due in 2013 out of the possible \$5 million in contingent payments under the Amended SPA. The parties reached agreement that the WTC Captive would pay the actual plaintiffs' portion of this \$3.8 million, or about \$2.85 million, according to the terms of the Amended SPA, setting aside the attorneys' fees and the remaining \$1.2 million to be addressed according to the results of the appeal. The agreement is without prejudice to either side's position in the appeal. As a result, \$3.8 million was placed into the settlement account on January 15, 2013. The \$2.85 million agreed to be due to individual plaintiffs was paid out on January 16, 2013 according to instructions from the Allocation Neutral, while fees of about \$950,000 subject to appeal remained in the settlement account. The remaining \$1.2 million of the \$5 million was placed into the separate account pending results of the appeal. In total, about \$48.7 million has been placed in a separate account relative to the bonus and contingent payment appeals. Briefing is complete on the consolidated appeals and oral argument was presented in April 2013. Corporate counsel argued on behalf of the WTC Captive and its insureds, and the questions focused on issues of contract interpretation. A ruling is expected in 2014.

In January 2014, the third contingent payment was due. Under the terms of the Amended SPA, the full \$5 million was owed. On February 3, 2014, WTC Captive paid the actual plaintiffs' portion of the \$5 million, or about \$3.8 million, according to the terms of the Amended SPA, setting aside the attorneys' fees of about \$1.2 million to be addressed according to the results of the appeal.



**WTC Captive Insurance Company, Inc.**  
**Notes to the Financial Statements**  
**As of and for the Years Ended December 31, 2013 and 2012**

**Note 7 - Contingencies (continued)**

Under the terms of its Bylaws, grant agreements and the Contract, the WTC Captive is authorized, and at certain times required, to evaluate the purchase of assumption reinsurance. Assumption reinsurance would provide the Company the ability to reinsure some or all of its obligations. With the resolution of essentially all claims against the Company's insureds, together with the reopening of the VCF, WTC Captive undertook its first such evaluation in 2013. Through the summer, WTC Captive undertook a competitive process to secure assumption reinsurance proposals. A Request for Proposal was developed, and eight global insurers were invited to compete for the opportunity. Two proposals were received, with one of the proposals offering terms most closely aligned with the Company's goals. These goals are straightforward: increased limits of financial protection for all insureds within a transaction structure that benefits all insureds while harming none; comparable coverage terms to the existing Contract; true assumption reinsurance that assigns all rights and obligation of the WTC Captive under the Contract to the new insurer; a demonstrated understanding by the assuming insurer of the unique provisions of the Contract; and an insurer who can provide long-term financial security for the WTC Captive's insureds. While the transaction was under regulatory review by NYSDFS and FEMA in November 2013, concerns raised by some members of Congress and by advocates for first responders put the transaction on hold. The transaction remains pending regulatory approval.

**Note 8 - Subsequent Events**

As noted in Note 5 and Note 7, the WTC Captive agreed to make annual payments of up to \$5 million per year for each of the first five years following the affirmation of final settlement, per the Amended SPA. The interpretation of this portion of the Amended SPA is currently on appeal to the US Court of Appeals for the Second Circuit. However, based on calculations according to the WTC Captive's appellate position, the full \$5 million was due in 2014. On February 3, 2014, WTC Captive paid the actual plaintiffs' portion of this \$5 million, or about \$3.8 million, according to the terms of the Amended SPA, setting aside the attorneys' fees of about \$1.2 million to be addressed according to the results of the appeal.



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**Report on Internal Control over Financial Reporting and on  
Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with Government Auditing Standards**

To the Board of Directors of  
WTC Captive Insurance Company, Inc.:

We have audited the financial statements of WTC Captive Insurance Company, Inc. ("WTC Captive" or the "Company") as of and for the year ended December 31, 2013, and have issued our report thereon dated March 10, 2014. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

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

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

**Compliance and Other Matters**

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

This report is intended solely for the information and use of the Board of Directors, management, and applicable federal, state, and city agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Saslow Lufkin & Buggy, LLP*

March 10, 2014  
Avon, CT



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**Independent Auditors' Reporting on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133**

To the Board of Directors of  
WTC Captive Insurance Company, Inc.:

**Compliance**

We have audited WTC Captive Insurance Company, Inc.'s ("WTC Captive" or the "Company") compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement*, that could have a direct and material effect on its major federal program for the year ended December 31, 2013. WTC Captive's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of WTC Captive's management. Our responsibility is to express an opinion on WTC Captive's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program occurred. An audit includes examining, on a test basis, evidence about WTC Captive's compliance with those requirements and performing such other procedures as considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide legal determination of WTC Captive's compliance with those requirements.

In our opinion, WTC Captive complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2013.

**Internal Control Over Compliance**

The Management of WTC Captive is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to the federal program. In planning and performing our audit, we considered WTC Captive's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, and to test and report on internal control over compliance in accordance with OMB Circular A-133 but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Company's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis.



Saslow Lufkin & Buggy, LLP

*Certified Public Accountants and Consultants*

A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with the type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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

This report is intended solely for the information and use of management, the Board of Directors, and others within the entity and applicable federal, state, and city agencies, and is not intended to be and should not be used by anyone other than these specified parties.

*Saslow Lufkin & Buggy, LLP*

March 10, 2014  
Avon, CT

**WTC Captive Insurance Company, Inc.**  
**Schedule of Expenditures of Federal Awards**  
**For the Year Ended December 31, 2013**

<b>Federal Grantor/Pass-through Grantor/Program or Cluster Title</b>	<b>Federal CFDA Number</b>	<b>Federal Expenditures (in thousands)</b>
Department of Homeland Security:		
Other pass-through entities for Federal Awards (see Note 1)		
Federal Emergency Management Agency		
New York State Office of Emergency Management		
New York City:		
Program Title: Debris Removal Insurance	97.064	\$ 26,590
Total Expenditures of Federal Awards		\$ 26,590

**WTC Captive Insurance Company, Inc.**  
**Note to the Schedule of Expenditures of Federal Awards**  
**For the Year Ended December 31, 2013**

**Note 1 - Basis of Presentation**

The accompanying schedule of expenditures of federal awards is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, “*Audits of States, Local Governments, and Non-Profit Organizations.*”

*(In thousands)*

Professional and management fees	\$ 3,400 *
General and administrative expenses	521
Personnel expenses	996
LAE - adjusting	6,744
LAE - all other	1,518
Settlement indemnity payments	4,331
Claim indemnity payments	<u>9,080</u>
Total expenditures of Federal Award	<u><u>\$ 26,590</u></u>

\* Amount includes investment management fees of \$413,000, which are netted against investment income in the *Statements of Activities* as of December 31, 2013.

**WTC Captive Insurance Company, Inc.**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended December 31, 2013**

***Section I - Summary of Auditors Results***

**Financial Statements**

Type of auditors' report issued:	<u>Unmodified</u>
Internal control over financial reporting:	
Material weakness identified?	<u>No</u>
Significant deficiency(ies) identified that are not considered to to be material weaknesses?	<u>None reported</u>
Noncompliance material to financial statements noted?	<u>No</u>

**Federal Awards**

Internal control over major program:	
Material weakness identified?	<u>No</u>
Significant deficiency(ies) identified that are not considered to be material weaknesses?	<u>None reported</u>
Type of auditors report issued on compliance for the major programs	<u>Unmodified</u>
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?	<u>No</u>
Identification of major program: CFDA - 97.064 - Establish captive insurance company for the coverage of various claims relating to the removal of debris as a result of the events of September 11, 2001.	
Dollar threshold used to distinguish between Type A and B programs: (greater of \$300,000 or 3% of expenditures of total awards, in thousands)	<u>\$ 797,700</u>
Does the audited qualify as low risk auditee?	<u>Yes</u>

***Section II - Financial Statement Findings Reported in Accordance  
with Generally Accepted Auditing Standards and Government  
Auditing Standards***

No matters were reported

***Section III - Federal Award Findings and Questioned Costs***

No matters were reported.