

MESSAGE FROM THE

President & Chairman



*Pamela E. Davis, President and CEO
and R. Lawrence Bacon, Chairman.*

While 2002 was a challenging year for nonprofits, the NIA Group served the sector well by holding a steady course during a period of great instability in the insurance marketplace. During the year our members were faced with cuts from funding sources, heightened service expectations, and greater demands for accountability. Add the rising cost for most types of commercial insurance, and it is safe to say that nonprofit organizations had a tough year. If there is any bright spot for us, it is knowing that Nonprofits' Insurance Alliance of California (NIAC) and the Alliance of Nonprofits for Insurance, Risk Retention Group (ANI-RRG), made this difficult time just a bit easier for 4,000 nonprofits.

For the NIA Group itself, the unstable marketplace resulted in higher costs for our reinsurance, despite our favorable claims record. As a consequence, we had our first price increase in our 13-year history. Although it was modest compared to increases for most buyers of commercial insurance, renewing members received average price increases of approximately nine percent on limits up to \$1 million. For members that purchased umbrella coverage with higher limits, we were less successful in negotiating reinsurance pricing.

NIAC has served nonprofits in California since 1989 and was expressly created to bring the sector through the type of insurance market we are presently experiencing. During

2002, despite some nonprofit consolidations and closings, NIAC renewed 93 percent of its member-insureds and welcomed 989 new members. NIAC has 892 members that have been continuously insured with us for five or more years, and 432 that have been with us for 10 or more years.

In early 1999, we noticed telltale signs that another insurance crisis might be looming for the commercial insurance industry. The steps we took to create ANI-RRG to serve nonprofits outside of California proved propitious. By late 2001, many commercial insurers were ceasing to write nonprofit business and others were dramatically increasing prices. Responding to this need, by the end of 2002 ANI-RRG was serving nonprofits in nine states and the District of Columbia. Growing at nearly three times NIAC's first-year pace, ANI-RRG completed its first full year with 369 member-insureds, including 297 new members.

On a combined basis, the NIA Group welcomed 1,286 new members and closed the year with 4,001 members. Gross written premium for the Group totaled \$35.4 million, an increase of 65 percent over the prior year. Net income of \$6.6 million was added to surplus to increase financial strength and to support future growth. At year-end, the NIA Group balance sheet showed total equity of \$38.3 million and total assets of \$94.6 million. Of the total gross written premium, \$30.9 million was written by NIAC and \$3.7 million by ANI-RRG.

Continued on page 2

The NONPROFITS INSURANCE ALLIANCE Group

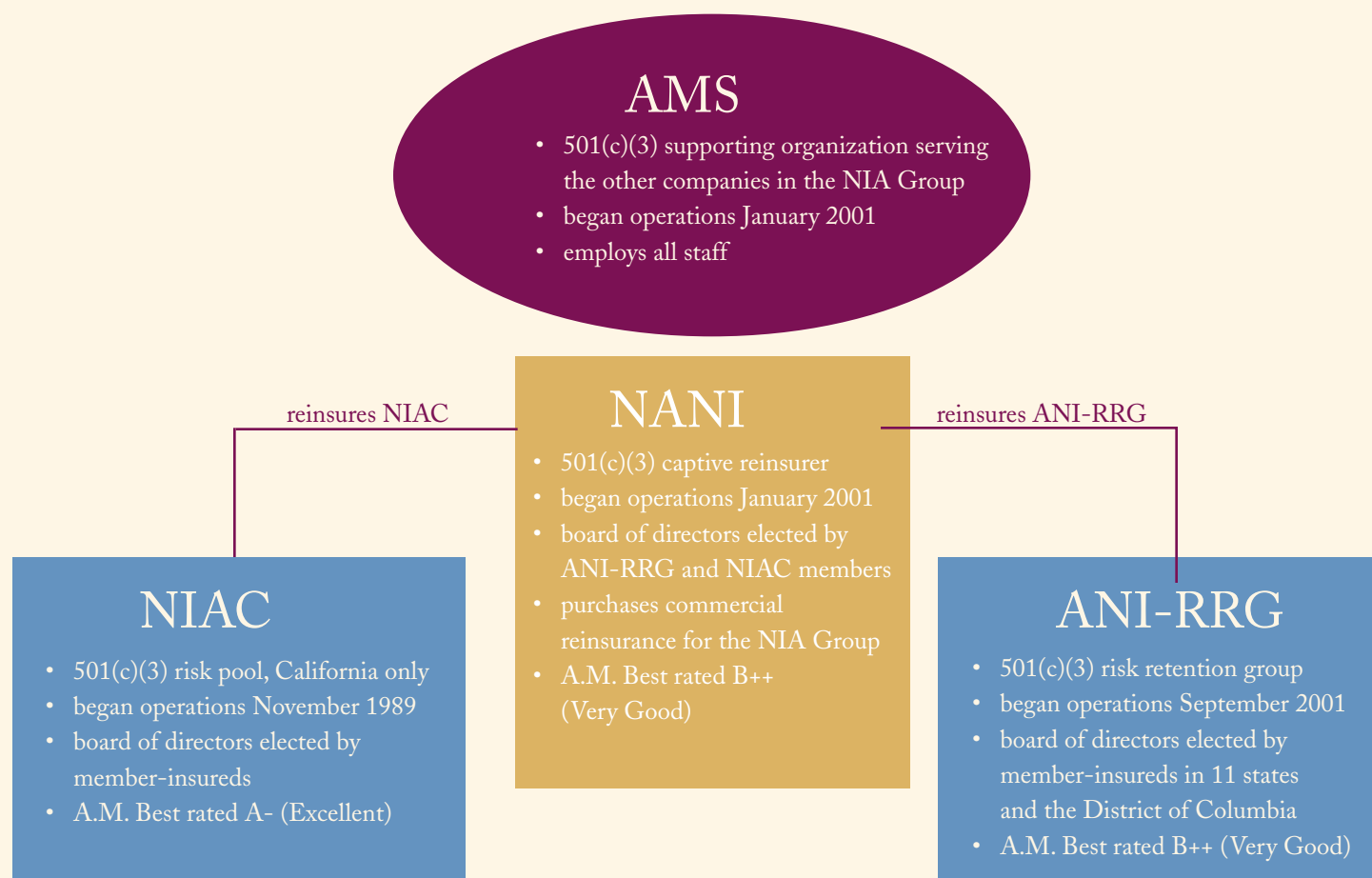
What started very simply as NIAC, one small company in one state, has grown into a sometimes confusing mix of acronyms—AMS, ANI-RRG, NANI and NIAC. These four distinct companies make up the Nonprofits Insurance Alliance Group (NIA Group). All of these organizations are 501(c)(3)

tax-exempt nonprofits governed by their nonprofit member-insureds.

We have provided an illustration below to help you understand how this group works together.

This structure enables one group of staff and management to serve nonprofits across the country, provides a vehicle for a nationwide

spread of risk, and allows the efficient development of loss control resources for members. The NIA Group has four independent, but related, boards of directors which share financial information, and which retain governance authority for their individual organizations in the NIA Group.



ANI-RRG = Alliance of Nonprofits for Insurance, Risk Retention Group

AMS = Alliance Member Services

NIAC = Nonprofits' Insurance Alliance of California

NANI = National Alliance of Nonprofits for Insurance

BOARDS OF DIRECTORS

NIAC



Back row (l-r):

R. Lawrence Bacon, Chair
President, Bacon and Company

William R. Ahern
Board Member, East Bay School for Girls

Nancy Johnston-Bellard
*Deputy Risk Manager
City and County of San Francisco*

Phillip Kimble
*Board Historian, Friendship Center
for the Blind*

Meredeth Clark
*President, CIS, a subsidiary
of California Association of Nonprofits*

Rocky A. Burks
*CEO, Independent Living Services
of Northern California*

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Janice L. Stout, SPHR
Human Resources Director, E Center

Ellis Kirschenbaum
*Senior Vice President
Children's Institute International*

Pamela E. Davis, President
Chief Executive Officer, NIAC

Richard J. Welch, ARM
*Director, Retired, Risk Management and Safety
City of Los Angeles*

Not Pictured:

John M. Christensen, Secretary
*Senior Vice President
Hope Rehabilitation Services*

Roger W. Gilbert, Treasurer
President, Retired, Great American West

Jack Shakely
*President
California Community Foundation*

ANI-RRG

Back row (l-r):

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Executive Vice President, Child, Inc., DE

Richard J. Welch, ARM
*Director, Retired, Risk Management and Safety
City of Los Angeles, CA*

Marianne P. Eby, Esq.
Acting CEO, BoardSource, DC

Robert D. Ridgeway
*Executive Director,
Providers' Resource Clearinghouse, CO*

Steven Richard
*COO & CFO,
SUN Home Health Services, Inc., PA*

Front row (l-r):

Audrey R. Alvarado, Ph.D.
*Executive Director, National Council
of Nonprofit Associations, DC*

Pamela E. Davis, President
Chief Executive Officer, ANI-RRG

Wilson M. Jones, Secretary
COO, Retired, BoardSource, DC

R. Lawrence Bacon, Chair
President, Bacon and Company, CA



Not Pictured:

Roger W. Gilbert, Treasurer
President, Retired, Great American West, CA

Andrew Sargeant, Assistant Secretary
President, USA Risk Group of Vermont, Inc., VT

STAFF



Back Row (l-r):

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Fred Rodriguez
Paul Roman
Jeff Ewart
Mike van Leynseele
Matt Dwyer
Bob Shane

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Chris Wafford
Vicki Campbell
Sandra Cornell
Michele Thomas
Sherri East
Tara Birnbaum
Mike Victor

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Marilyn McCoun
Kathleen Palmer
Mandy Hargens
Sati D'Alessandro
Livia Peras
Calley Bryce

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Sean Kelly
Randy Gorman
Cindy Marshall
Dawn Mueller
Claudia Weeks

Row Two (l-r):

Jan Kirschner
Kim Aday
Stephanie Villarreal
Heather Gray
Vikki Sanders
Shaneen Takaki

Not Pictured:

Dusti McKeown
Leah Price

Front Row(l-r):

Michael Pramuk
Bonnie Williams
Julie Bernhard
Dottie Lechtenberg

MANAGEMENT TEAM



Back row (l-r):

Sam Koriakos, CPA
Vice President, CFO

Lola Hogan, CPCU ARM
Vice President Claims

Steven Moody
Vice President
Insurance Operations

Front row (l-r):

Betty Johnson
Vice President
Information Technology

Pamela E. Davis
President and CEO

Susan Bradshaw
Vice President
Marketing/Member Services

How We're Different...



LIVING FREE ANIMAL SANCTUARY, CANOGA PARK, CA—A NIAC member since 1998. Living Free rescues adult cats and dogs scheduled for pound euthanasia and places them in loving adoptive homes. Due to the strained economy and reduced donations, they recently had to sell the mountain acreage where this sanctuary has operated for more than 22 years, but they are determined to continue their mission in a new location.

Because we're nonprofits too, we understand nonprofits' unique insurance needs. We know that nonprofits work on tight budgets and that instability in the insurance market can have a negative impact on their financials and mission.

In 2002, the insurance industry faced a financial crisis much like the insurance crisis in the mid-1980s. During the 1980s crisis, many nonprofits in California could not obtain insurance at any price. The Nonprofits' Insurance Alliance of California (NIAC) was created as a result of that crisis and now insures more than 3,600 nonprofits across California.

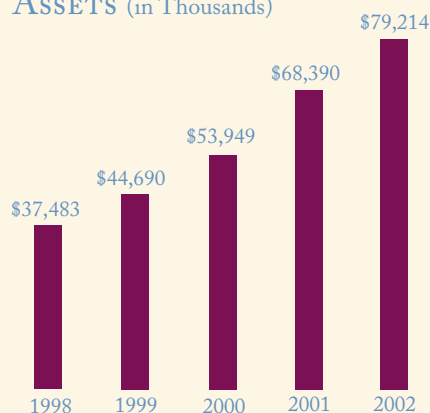
The Alliance of Nonprofits for Insurance, Risk Retention Group (ANI-RRG) was the outcome of a 1999 feasibility study, underwritten by the David and Lucile Packard Foundation to determine what it would take to expand NIAC's concept nationwide. ANI-RRG

was incorporated in 1999, began operations in September 2001 and currently insures more than 400 nonprofits. As of this March 2003 publication, ANI-RRG is currently writing business in Colorado, Delaware, Kansas, Maryland, Michigan, Nevada, North Carolina, Ohio, Oregon, Pennsylvania, Virginia and the District of Columbia. In 2003, ANI-RRG expects to expand into Iowa, Missouri, Minnesota, Nebraska, Utah and Washington.

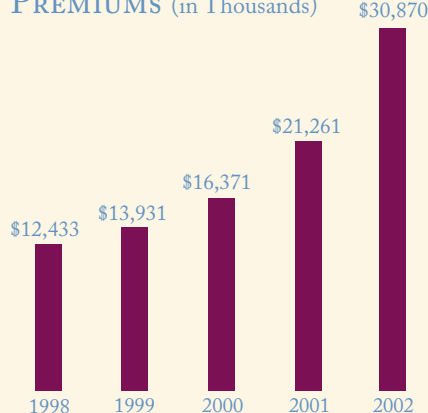
Initial capital for ANI-RRG was provided by \$10 million in grants from the David and Lucile Packard Foundation and the Bill & Melinda Gates Foundation. Each foundation contributed \$5 million in capital for ANI-RRG and an affiliated company, the National Alliance of Nonprofits for Insurance (NANI), a captive reinsurer. NANI provides reinsurance to ANI-RRG and NIAC and is itself presently reinsured by Swiss Re, A.M. Best rated A++.

NIAC

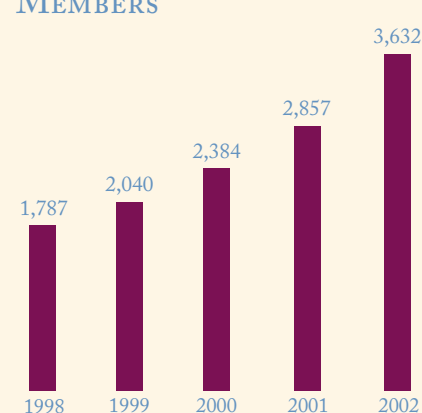
ASSETS (in Thousands)



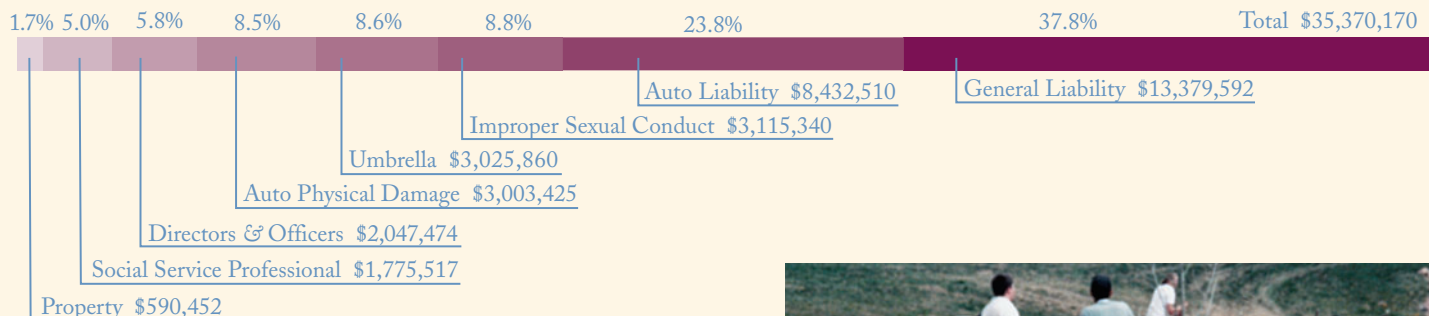
PREMIUMS (in Thousands)



MEMBERS



2002 PREMIUM BY LINE (NIA Group Combined)



All of these affiliated companies, known as the Nonprofits Insurance Alliance Group (NIA Group), are also 501(c)(3) tax-exempt organizations governed by boards elected by their nonprofit member-insureds. All have related boards of directors elected annually by member nonprofits and all exist only to serve 501(c)(3) tax-exempt nonprofits.

In 2002, in recognition of her role as founder, president and CEO of the member companies of the NIA Group, *The Nonprofit Times* named Pamela Davis to the list of the Top 50 Nonprofit Leaders in the nation.

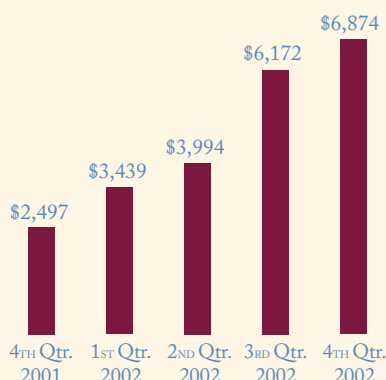
As stated in the *Times*, "Davis is one of the first social entrepreneurs, leveraging venture capital from foundations to impact public policy and help nonprofits gain a measure of control over a vital financial service." We are proud of this honor both for Pamela individually and for the acknowledgment of the contributions of the NIA Group of companies to the well-being of the nonprofit sector.



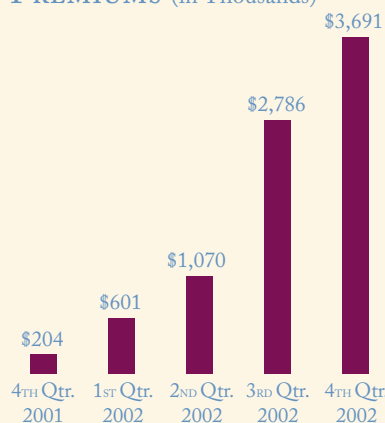
TREES, WATER AND PEOPLE, FORT COLLINS, CO
—An ANI-RRG member since 2002. *Trees, Water and People* is dedicated to working cooperatively with communities and other organizations to protect the sustainability of forests and watersheds. They believe that natural resources are best protected when local people play an active role in their care and management.

ANI-RRG

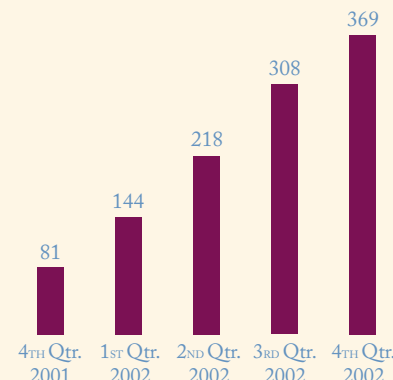
ASSETS (in Thousands)



PREMIUMS (in Thousands)



MEMBERS



MEMBER SERVICES



LoDo DISTRICT, DENVER, CO —An ANI-RRG member since 2002. The LoDo District strives to preserve, promote and represent the Lower Downtown Historic District. Through their LoDo Cares program, residents of the Barth Hotel (like the woman pictured above), receive Christmas and birthday gifts, and donations of items such as powder and nice soap, which would otherwise not be affordable for these residents.

Part of our mission is to provide members with risk management and loss control resources and services. Being proactive and providing practical and user-friendly risk management and loss control tools is much more satisfying and cost-effective than paying claims for preventable accidents and injuries. These resources for member-insureds are free or highly subsidized. Some of the products and services provided in 2002 include:

EDUCATIONAL BOOKLETS

Nine booklets (available free on the website and in print) are currently available, covering topics such as special events, directors and officers insurance, what nonprofits need to know about lawsuits, managing volunteers, surviving a crisis, tips for vehicle safety programs, avoiding sexual abuse, managing collaboration risks and managing technology risks. Each booklet explores liability issues faced by most nonprofits, and has been written specifically for the nonprofit reader. Many case studies and sample forms are available in each booklet.

DRIVER TRAINING

Driver training classes are provided free of charge to members that purchase commercial auto insurance from us. During 2002, more than 650 drivers were trained throughout California and 85 drivers were trained in the initial year of offering this service to ANI-RRG members.

D&O ATTORNEY ADVICE

For members with a directors and officers policy with NIAC or ANI-RRG, this resource offers free pre-termination consultation with a labor law attorney. In 2002, 215 members took advantage of this service. These consultations helped our members avoid the most common errors in terminating employees, and as a result, helped avoid many expensive and time consuming lawsuits.

NONPROFIT CARES

(Computer Assisted Risk Evaluation System)—NIAC Edition. In cooperation with the Nonprofit Risk Management Center, we developed an interactive CD-Rom risk assessment tool for California nonprofits. Six modules include the following topics: Introduction to Risk Management, Transportation, Contracts, Harm to Clients, Special Events and Employment Practices. We also make available a subsidized copy of the nationwide version to ANI-RRG members.

"The lending library is a valuable resource to our agency, and I really appreciate the services you provide."

—Florence LeFrancois
Sierra Adoption Services
Nevada City, California

VIDEO LENDING LIBRARY

To complement their internal training programs, members can take advantage of our video lending library, a valuable resource for our members. Topics range from driver safety and employment practices to the prevention of sexual abuse. New titles are being added to the library on a regular basis.

WEB SITES

Members may order publications and videos on-line, and much of the loss control material may be downloaded. Visit our web sites at www.InsuranceforNonprofits.org.

WORKSHOPS

We continue to sponsor educational events, and to serve as a resource for insurance and risk management information for nonprofits. In 2002, staff made many presentations for nonprofit support organizations such as Nonprofit Risk Management Center, Nonprofit Support Center of Santa Barbara County, Ohio Association of Nonprofit Organizations, and Marin Nexus, to name just a few.

NEWSLETTERS

Three newsletters were distributed to members in 2002. Topics included avoiding claims and lawsuits, and employment issues. In 2003, the Alliance Report will be delivered electronically.

CLAIMS

And last, but certainly not least is the extensive service we provide for members during the handling of claims. We never consider the claims process routine. We understand that a poorly handled lawsuit can have a negative impact on a nonprofit's standing in the community and its ability to raise funds.

We aggressively investigate claims made against our nonprofit members. While we strongly resist paying frivolous or inflated claims, we also avoid needless legal wrangling when liability is clear and the demand is reasonable. We believe these practices save our members money and preserve their good names.

"There will never be enough time, opportunity or 'thank you's' to cover how grateful I feel for the expertise, understanding and loyalty you provided us in handling our claim during this very difficult period."

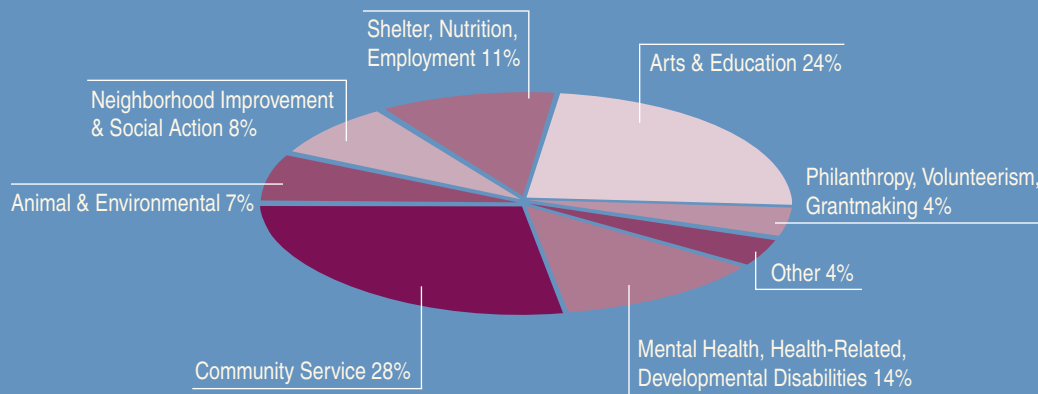
—John J. Nelson
Extended Child Care
Santa Rosa, California



CHILDREN TODAY, LONG BEACH, CA —A NIAC member since 2000. Children Today's mission is to increase the safety and nurturing of children from homeless families by providing quality child care services free of charge. Their Play House provides homeless children with basic needs—a safe environment, nutritious meals and snacks, health care services, and specially-trained loving, nurturing caregivers.

MEET OUR MEMBERS

2002 Member Composition



ANI-RRG and NIAC serve a broad array of 501(c)(3) non-profit organizations such as boys and girls programs, animal rescue operations, group homes, senior organizations, theater groups, food banks, community groups and others. Today, nonprofits are facing cutbacks in government funding, grants and contributions while the need for their services increases. We are proud to be associated with the organizations that make up this important sector and do our best to support their efforts by providing them with appropriate insurance coverages and risk management tools to protect their organizations and their clients.

To learn more about the diverse group of nonprofits that comprise our membership, take a few moments to read the following member profiles. A complete list of members (as of 12/31/2002) is furnished in the pocket of this report.



SAN LUIS OBISPO CHILDREN'S MUSEUM, SAN LUIS OBISPO, CA—A NIAC member since 1992. The Museum offers more than 25 hands-on exhibits to stimulate imagination and play between children and their adult companions. Pictured here, a group of kids try out some fireman hats and other costumes.

"...After the crisis we faced with the 2002 renewals of our liability insurance, ANI-RRG felt unbelievable, but...we continue to be amazed. The cost savings are tremendous, but equally important ...we feel a better sense of partnership receiving our insurance services through another nonprofit organization."

—Marcus Games
Sojourners Care Network
McArthur, Ohio

MEMBER PROFILES



SENIOR DAY CARE CENTER SAN JACINTO, CA

The Senior Day Care Center of Hemet-San Jacinto provides care and services for the frail elderly and chronically ill patients of the Hemet-San Jacinto area, as well as respite for their caregivers.

The Center offers a safe, protected environment where patients can be cared for while their regular caregivers are at work or are enjoying some respite time. Balanced hot lunches and snacks are served and activities include chair exercises, arts and crafts, word games, coordination games and sing-alongs.

Twenty years ago, the Center was founded when the concept of senior day care was a new one and there were no other options available in the area. Caregivers often become overwhelmed with the task of caring for their loved one. Even just a few short hours of respite per week can make a huge difference for a caregiver. The Center also facilitates a support group for caregivers twice a month.

The Senior Day Care Center of Hemet-San Jacinto has been a NIAC member since 1992.

HEMOPHILIA FOUNDATION OF MICHIGAN ANN ARBOR, MI

The Hemophilia Foundation of Michigan provides programs and services for individuals and families in the hereditary bleeding disorders community with the ultimate goal of finding a cure.

HFM offers a variety of educational services, including workshops, meetings, symposiums and numerous publications and informational materials. The agency also coordinates the funding, professional education and networking for hemophilia treatment centers located in hospitals throughout the state.

Since 1969, HFM has offered a residential youth camping program for children with hereditary bleeding disorders in recognition of their

special needs. This program includes traditional camping activities as well as a 24-hour staffed clinic. These camps provide challenging and safe experiences for children traditionally excluded from summer camping programs. Activities include hiking and nature exploration, canoeing, archery and swimming. It also gives the kids an opportunity to meet other children with similar life experiences.

HFM offers many other services to the community,

such as telephone counseling, financial assistance, and information and referral services.

The Hemophilia Foundation of Michigan has been an ANI-RRG member since 2002.



MEMBER PROFILES



PROJECT INDEPENDENCE COSTA MESA, CA

Project Independence promotes community integration of persons with developmental disabilities and creates services which expand their opportunities for personal freedom and choice.

They offer an independent living services program which assists individuals who live in their own apartments, and a supported living program which has the option of paid roommates or 24-hour support. The agency also offers a supported employment services program which matches community jobs with clients

who are able and eager to work. This service offers career planning, on-site job training and ongoing case management.

Other programs Project Independence offers include community skills training, transportation training, and special group trips to such destinations as New York, Hawaii and Mexico. Pictured at left is a participant in the yacht racing team. Other teams include a mountaineering team and bowling tournament.

Project Independence has been a NIAC member since 1997.

COMMUNITY FOOD SHARE LONGMONT, CO

Community Food Share, now in its 22nd year of operation, works through a network of 90 human service agencies at 177 sites to collect, produce, and distribute food to the hungry in Boulder and Broomfield, Colorado communities. In 2002, CFS distributed more than 1.8 million pounds of food to those in need in their community. CFS is an affiliate of America's Second Harvest, a national network of food banks dedicated to ending the problem of domestic hunger.

The food that CFS distributes is collected from private local donors, manufacturers, grocers, retailers and restaurants. Five major food drives throughout the year provide more

than 20% of their food needs. Fresh produce is collected through partnerships with local farmers who donate leftover product after their harvest. Their gleaning program supplies more than 50,000 pounds of fresh produce annually.

The food is distributed with the help of partner agencies, as well as through CFS direct-to-client initiatives such as Elder Share, which provides supplemental groceries bi-monthly to senior citizens,

and the "Mobile Food Panty," which provides monthly food distribution in neighborhoods of high need.

Community Food Share has been an ANI-RRG member since 2002.



MEMBER PROFILES

GOODWILL INDUSTRIES OF DELAWARE & DELAWARE COUNTY WILMINGTON, DE

Goodwill Industries of Delaware & Delaware County employs more than 400 individuals, 70-85% of whom have a disability or other barrier to employment, such as welfare dependency, homelessness, lack of education or work experience. Since 1921, the agency's intent has been to give individuals a "hand up, not a hand out," so they may experience the dignity of self-sufficiency.

In addition to its thrift stores, Goodwill operates a computer recycling center, a janitorial service, a

staffing service, and an industrial contracts service.

Goodwill's job training programs teach marketable skills like the food service training program (pictured here). Goodwill also provides classes in resume writing, interview skills, and "soft-skills" needed for success on the job. After graduation, Goodwill assists the students with job placement and offers retention assistance and follow-up to ensure success.

Goodwill Industries of Delaware & Delaware County has been an ANI-RRG member since 2001.



WILDLIFE FAWN RESCUE KENWOOD, CA

Wildlife Fawn Rescue is the only facility in Sonoma County that specializes in the rehabilitation of Black-tailed fawns. The all-volunteer staff gives intensive care to nearly one hundred

fawns per year, in addition to other kinds of wildlife.

Fawns are received from the Department of Fish and Game, local vets, Animal Control, Humane Society, animal emergency centers,

other wildlife centers and from the public. If any injury or illness is evident, the animal is taken to a veterinarian. The fawns are enclosed in a natural environment where they are exposed to the native wildlife they will eventually rejoin. After they are fully weaned and are

well, fawns are released on private land with permission of the owners.

The volunteers also strive to educate the public about fawns and wild animal hazards. Baby animals that are left alone while their mothers forage for food are often picked up by humans who mistakenly think they have been abandoned. Wildlife Fawn Rescue educates the public to never move an animal, but rather to call a wildlife expert if the animal appears injured.

Wildlife Fawn Rescue has been a NIAC member since 2002.



MEMBER PROFILES



THE COMMUNITY MUSIC SCHOOL OF SANTA CRUZ SANTA CRUZ, CA

The Community Music School of Santa Cruz encourages and supports opportunities in their community to explore the varieties of musical experience.

The Music School serves as a resource bank to connect potential students with private instructors for instruments ranging from guitar and piano to bagpipes and folk harps. They also sponsor the living history concert series, providing educational concerts to the public at low-cost.

Each year, the Music School organizes a number of music workshops

and sponsors two Celtic music camps for children and teens in a beautiful redwood forest setting.

Pictured at left is a group of teen campers rehearsing traditional Celtic music. Each day of the week-long camp, the participants enjoy outdoor activities as well as musical instruction. At night there are a variety of activities with expert guest instructors, and performances that highlight the camper's new skills.

The Community Music School of Santa Cruz has been a NIAC member since 1999.

TOLEDO URBAN IMPACT TOLEDO, OH

Toledo Urban Impact was founded by a couple who wanted to offer hope to kids in the inner-city neighborhoods of Central Toledo. Their vision was to encourage one child at a time to rise above their circumstances and achieve their fullest potential. The program is based on these one-on-one relationships between caring adult volunteers and children in need. Many of these kids would not otherwise experience this level of personal involvement with an adult who is focused on helping them meet their goals.

Pictured at right, the ASK (After-School Klub) program provides homework assistance, tutoring,

supervised recreation and healthy snacks two afternoons a week for children in grades four through eight.

Through the mentoring program, adults meet weekly with a child and develop a nurturing relationship. The program also offers sponsorships for summer and school-year camps to kids who would otherwise not have that opportunity.

Gift baskets are offered at the beginning of the school year and during the holi-

days. Home visits by volunteers also encourage parents to be involved in their kids lives and their choices.

Toledo Urban Impact has been an ANI-RRG member since 2002.



INDEPENDENT AUDITORS' REPORT



TO THE BOARD OF DIRECTORS OF NONPROFITS INSURANCE ALLIANCE GROUP:

In our opinion, the accompanying combined balance sheet as of December 31, 2002 and the related statements of income and changes in total equity and cash flows present fairly, in all material respects, the financial position of Nonprofits Insurance Alliance Group at December 31, 2002, and the changes in its total equity and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we

plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion. The financial statements of the Company as of December 31, 2001 and for the year then ended were audited by other independent accountants whose report dated March 8, 2002 expressed an unqualified opinion on those statements.

PRICEWATERHOUSECOOPERS LLP

March 7, 2003

Nonprofits Insurance Alliance Group

COMBINED BALANCE SHEETS

	2002	2001
<i>Assets</i>		
Cash and investments:		
Cash	\$ 2,445,915	\$ 723,303
Investments (cost: 2002 - \$59,974,541; 2001 - \$51,215,131)	<u>61,117,252</u>	<u>51,999,385</u>
Total cash and investments	63,563,167	52,722,688
Premiums receivable, net of allowance for doubtful accounts of \$1,133 in 2002 and \$7,299 in 2001	7,975,296	4,618,395
Interest receivable	484,381	530,132
Other receivable	260,990	
Prepaid expenses and other assets	143,631	111,321
Reinsurance recoverables	8,104,202	8,702,759
Prepaid reinsurance premium	4,054,673	1,747,430
Deferred acquisition costs	3,136,653	1,831,503
Assets held in trust		35,043
Property and equipment, net of accumulated depreciation of \$966,156 in 2002 and \$564,546 in 2001	<u>6,848,193</u>	<u>6,496,872</u>
Total assets	<u>\$ 94,571,186</u>	<u>\$ 76,796,143</u>
<i>Liabilities and Equity</i>		
Liabilities:		
Loss and loss adjustment expense reserves	\$ 31,922,530	\$ 25,538,201
Accounts payable and other accrued liabilities	1,404,233	2,207,264
Unearned premiums	17,260,092	9,772,713
Reinsurance payable	1,403,006	2,898,494
Loans payable	<u>4,240,734</u>	<u>4,405,000</u>
Total liabilities	56,230,595	44,821,672
Total equity - unrestricted:		
Members' contributions	900,507	900,507
Capital contribution	10,000,000	10,000,000
Accumulated earnings	26,297,373	20,290,361
Unrealized gains on investments, net	<u>1,142,711</u>	<u>783,603</u>
Total equity - unrestricted	<u>38,340,591</u>	<u>31,974,471</u>
Total	<u>\$ 94,571,186</u>	<u>\$ 76,796,143</u>

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

Nonprofits Insurance Alliance Group

COMBINED STATEMENTS OF INCOME AND CHANGES IN TOTAL EQUITY

	2002	2001
<i>Revenues</i>		
Gross written premium	\$ 35,370,170	\$ 21,476,428
Ceded premium	<u>(6,802,461)</u>	<u>(3,826,878)</u>
Net written premium	28,567,709	17,649,550
Increase in unearned premium, net	<u>(5,180,136)</u>	<u>(1,925,928)</u>
Net earned premium	23,387,573	15,723,622
Net investment income	2,091,750	2,469,807
Net realized gain on sales of investments	1,405,560	158,216
Other income	<u>1,668,115</u>	<u>1,316,011</u>
Total revenues	<u>28,552,998</u>	<u>19,667,656</u>
<i>Expenses</i>		
Losses and loss adjustment expenses incurred	14,148,063	7,489,971
Salaries and employee benefits	2,858,648	3,061,575
Commission expense	2,783,099	2,499,247
Other expense	<u>2,158,011</u>	<u>214,018</u>
Total expenses	<u>21,947,821</u>	<u>13,264,811</u>
Net income	6,605,177	6,402,845
<i>Other changes in total equity</i>		
Capital contribution		5,000,000
Return of premium	(598,165)	
Change in net unrealized gains on investments	<u>359,108</u>	<u>428,261</u>
	6,366,120	11,831,106
Total equity - unrestricted, beginning of year	<u>31,974,471</u>	<u>20,143,365</u>
Total equity - unrestricted, end of year	<u>\$ 38,340,591</u>	<u>\$ 31,974,471</u>

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

Nonprofits Insurance Alliance Group

COMBINED STATEMENTS OF CASH FLOWS

	2002	2001
<i>Cash flows from operating activities</i>		
Net income	\$ 6,605,177	\$ 6,402,845
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized gains on investments	(1,405,560)	(158,216)
Depreciation and amortization	485,921	339,429
Amortization of premium of debt securities	44,294	88,623
Changes in assets and liabilities:		
Premiums receivable	(3,356,901)	(1,879,510)
Interest receivable	45,751	(61,454)
Other receivable	(260,990)	
Prepaid expenses and other assets	(32,310)	(30,109)
Reinsurance recoverable	598,557	(2,379,460)
Prepaid reinsurance premium	(2,307,243)	(290,990)
Deferred acquisitions costs	(1,305,150)	(367,832)
Assets held in trust	35,043	785,129
Loss and loss adjustment expense reserves	3,849,949	4,374,330
Unearned premiums	7,487,379	2,216,919
Reinsurance payable	(1,495,488)	1,626,228
Accounts payable and other accrued liabilities	(803,031)	(18,463)
Net cash provided by operating activities	<u>10,719,778</u>	<u>10,647,469</u>
<i>Cash flows from investing activities</i>		
Purchase of investments	(246,784,957)	(105,804,059)
Sales and maturities of investments	239,387,492	92,789,807
Purchases of property and equipment	(837,270)	(1,707,391)
Net cash used in investing activities	<u>(8,234,735)</u>	<u>(14,721,643)</u>
<i>Cash flows from financing activities</i>		
Proceeds from capital contributions		5,000,000
Subordinated debt principal repayment		(155,600)
Return of premium	(598,165)	
Repayment of loans payable	(164,266)	(155,000)
Net cash provided by financing activities	<u>(762,431)</u>	<u>4,689,400</u>
Net increase in cash	1,722,612	615,226
Cash, beginning of year	<u>723,303</u>	<u>108,077</u>
Cash, end of year	<u>\$ 2,445,915</u>	<u>\$ 723,303</u>
<i>Supplemental disclosure of cash flow information</i>		
Capitalized interest expense	\$ <u> </u>	\$ <u>42,802</u>
Cash paid for interest expense	\$ <u>106,328</u>	\$ <u>90,441</u>
Transfer of Restricted Investments to Unrestricted Investments	\$ <u> </u>	\$ <u>1,232,710</u>

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

NOTES TO COMBINED FINANCIAL STATEMENTS

I. ORGANIZATION

Nonprofits Insurance Alliance Group (the “Group”) consists of nonprofit companies whose primary activities include serving 501(c)(3) tax-exempt nonprofit organizations by providing a stable source of reasonably priced liability insurance coverage tailored to the specialized needs of the nonprofit sector, and assisting these organizations to develop and implement successful loss control and risk management programs. The Group includes Nonprofits Insurance Alliance of California, Inc. (“NIAC”), Alliance of Nonprofits for Insurance, Risk Retention Group, Inc. (“ANI-RRG”), National Alliance of Nonprofits for Insurance, Inc. (“NANI”), and Alliance Management Services, Inc. (“AMS”).

NIAC operates as a risk pool in California pursuant to authorization under Section 5005.1 of the California Corporations Code. NIAC provides commercial general liability, social service professional liability, automobile liability, auto physical damage, employer’s non-owned and hired auto liability, improper sexual conduct and directors and officers liability and umbrella liability coverage to its members.

ANI-RRG and NANI operate as captive insurance companies in Vermont pursuant to authorization under 8 V.S.A., Section 6002, and are subject to the rules, regulation and supervision of the Vermont Department of Banking, Insurance, Securities, and Health Care Administration. ANI-RRG provides commercial general liability, social service professional liability, employee benefits liability, business auto liability, and non-owned and hired automobile liability, improper sexual conduct liability, directors and officers liability and umbrella liability coverage to its members. NANI provides reinsurance to affiliates in the Group and certain other carriers providing coverage for NIAC and ANI-RRG members. The capital contributions to ANI-RRG of \$1,000,000 in 2001 and to NANI of \$4,000,000 in 2001 were provided by Bill & Melinda Gates Foundation and David and Lucile Packard Foundation.

The Group does not participate in insurance guarantee associations, state organizations that guarantee certain payments to claimants in the event of an insolvency of a regulated insurer.

AMS is a nonprofit company incorporated in Vermont to provide management services to affiliates in the Group and is responsible for their overall operation, including policy services, claim management, member services, reinsurance negotiations, marketing, accounting and financial management, and general and administration management.

On January 1, 2001, NIAC transferred its employees and its employment obligations and related assets and liabilities, including its sponsorship of the 401(k) plan, to AMS. AMS recorded the assets and liabilities at the carrying amount in the accounts of NIAC at the time of transfer.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying combined financial statements include the accounts of NIAC, ANI-RRG, NANI and AMS. The financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America. All balances and transactions between the companies have been eliminated in combination. The Group follows accounting and reporting policies for insurance enterprises.

Financial statement estimates

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

Revenue recognition

Premiums are recognized as earned on a pro rata basis over the terms of the policies, usually twelve months. Unearned premiums reserves are established to cover the unexpired portion of premiums written.

Deferred acquisition costs

Policy acquisition costs incurred are deferred and amortized over the period of premium recognition. These costs generally include commissions, underwriting, policy issuance and marketing costs. Amortization of acquisition costs was \$4,275,578 for 2002 and \$3,889,676 for 2001. Anticipated investment income is not considered in determining if a premium deficiency exists.

Property and equipment

Data processing equipment, purchased software, costs for internal-use software and office furniture and equipment are stated at cost, net of accumulated depreciation, and depreciated over five years using the straight-line method. Building is stated at cost, net of accumulated depreciation, and depreciated over 40 years using the straight-line method. Land is stated at historical cost. Upon retirement or disposition of property and equipment, any gain or loss is included in income.

Investments

Investments are classified as available-for-sale securities and are reported at market value, with unrealized gains and losses excluded from operating earnings and reported as a separate component of total equity. Fair value of equity securities is estimated by using quoted market prices for most securities. Estimated fair values of debt securities are based on average bid prices, or for newly issued securities, the average bid prices of similar issues with the same life and expected yields. Declines in the fair value of investments which are determined to be other than temporary, are included in net

investment income as a realized loss. Net realized investment gains or losses are recognized based upon the specific identification of investments sold. The Group has investments in commercial paper. Although such investments meet the criteria for cash equivalents, the Group has elected to include commercial paper in investments. Cash consists of cash deposits at banks.

Liability for Losses and Loss Adjustment Expenses ("LAE")

The liability for losses and LAE consists of estimated costs of each unpaid claim reported prior to the close of the accounting period, as well as those incurred but not yet reported. Management and the Group's consulting actuary believe that the reserves for losses and LAE at December 31, 2002 and 2001 are appropriately established in the aggregate and adequate to cover the ultimate net cost of reported and unreported claims arising from losses which had occurred by that date. The establishment of appropriate reserves is an inherently uncertain process.

Such reserves are necessarily based on estimates and the ultimate net cost may vary from such estimates. These estimates are regularly reviewed and updated using the most current information available. Any resulting adjustments, which may be material, are reflected in current operations.

Reinsurance

Reinsurance recoverables (including amounts related to claims incurred but not reported) and prepaid reinsurance premiums are reported as assets. Estimated reinsurance recoverables are recognized in a manner consistent with the liabilities relating to the underlying insured contracts.

Income taxes

The companies in the Group are tax-exempt for federal tax purposes under Section 501(c)(3) of the Internal Revenue Code.

Estimated fair value of financial instruments

The carrying value of cash, premiums receivable and reinsurance payable approximate their estimated fair value. Fair value of the loan payable is estimated to be carrying value, as the loan has a variable interest rate.

Reclassifications

Certain 2001 amounts have been reclassified to conform to 2002 presentation. These reclassifications have had no effect on net income or total equity.

3. INVESTMENTS

Unrestricted investments, carried in the accompanying balance sheets at estimated fair value, consist of the following as of December 31, 2002 and 2001:

	Cost or Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
2002				
Corporate obligations	\$ 11,948,274	\$ 395,406	\$	\$ 12,343,680
U.S. government and agency obligations	25,621,979	595,085	429	26,216,635
Mortgage-backed securities	16,130,459	153,652	33,462	16,250,649
Asset-backed securities	4,222,786	39,957	6,752	4,255,991
Other debt securities	<u>525,954</u>	<u>22,998</u>		<u>548,952</u>
Total debt securities	58,449,452	1,207,098	40,643	59,615,907
Equity securities	665,084	15,425	39,169	641,340
Money market account	<u>860,005</u>			<u>860,005</u>
Total investments	<u>\$ 59,974,541</u>	<u>\$ 1,222,523</u>	<u>\$ 79,812</u>	<u>\$ 61,117,252</u>
	Cost or Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
2001				
Corporate obligations	\$ 15,592,356	\$ 424,555	\$ 10,759	\$ 16,006,152
U.S. government and agency obligations	18,448,669	237,492	71,262	18,614,899
Mortgage-backed securities	7,744,847	76,773	16,095	7,805,525
Asset-backed securities	6,502,221	120,996		6,623,217
Other debt securities	<u>1,599,258</u>	<u>110</u>		<u>1,599,368</u>
Total debt securities	49,887,351	859,926	98,116	50,649,161
Equity securities	880,000	52,727	30,283	902,444
Money market account	<u>447,780</u>			<u>447,780</u>
Total investments	<u>\$ 51,215,131</u>	<u>\$ 912,653</u>	<u>\$ 128,399</u>	<u>\$ 51,999,385</u>

The amortized cost and estimated fair value of unrestricted investments at December 31, 2002 and 2001, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or repayment penalties.

	2002	
	Cost or Amortized Cost	Estimated Fair Value
Due in 1 year or less	\$ 11,402,333	\$ 11,401,529
Due after 1 year through 5 years	19,133,556	21,737,821
Due after 5 years	7,560,318	5,969,917
Mortgage-backed securities	16,130,459	16,250,649
Asset-backed securities	4,222,786	4,255,991
Total	<u>\$ 58,449,452</u>	<u>\$ 59,615,907</u>

Gross realized gains and losses on sales of fixed maturity securities were \$2,503,770 and \$362,839 in 2002, respectively, and \$693,114 and \$285,884 in 2001, respectively. Gross realized gains losses on sales of equity securities were \$28,292 and \$217,379 in 2002, respectively, and \$71,452 and \$320,466 in 2001, respectively. In addition, in 2002, a realized loss of \$500,000 was recognized on a fixed income security and realized losses of \$46,283 were recognized on equity securities, that were considered other than temporarily impaired in value.

Based on the requirement of the Vermont Department of Banking, Insurance, Securities, and Health Care Administration, ANI-RRG and NANI have maintained at least \$500,000 and \$750,000, respectively, of investment in U.S. Treasury Bills in 2002.

4. PROPERTY AND EQUIPMENT

Property and equipment at December 31 consists of:

	2002	2001
Computer and software	\$ 1,092,633	\$ 801,322
Furniture and fixtures	150,500	140,588
Internal software	1,846,838	1,460,405
Land	900,000	900,000
Building	<u>3,824,378</u>	<u>3,759,103</u>
Total	7,814,349	7,061,418
Accumulated depreciation	<u>(966,156)</u>	<u>(564,546)</u>
Property and equipment, net	<u>\$ 6,848,193</u>	<u>\$ 6,496,872</u>

Depreciation expense of \$485,921 and \$339,429, including amortization of leasehold improvements, was recognized for the years ended December 31, 2002 and 2001, respectively.

5. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

Activity in the loss and loss adjustment expense reserves is summarized as follows:

	2002	2001
Gross loss and loss adjustment expense reserves, January 1	\$ 25,538,201	\$ 22,924,752
Reinsurance recoverables	<u>(8,702,759)</u>	<u>(8,084,180)</u>
Net loss and loss adjustment expense reserves	16,835,442	14,840,572
Incurred related to:		
Current year	16,211,256	10,633,001
Prior years	<u>(2,063,193)</u>	<u>(3,143,030)</u>
Total incurred	14,148,063	7,489,971
Paid related to:		
Current year	2,531,173	1,596,727
Prior years	<u>4,634,004</u>	<u>3,898,374</u>
Total paid	7,165,177	5,495,101
Net loss and loss adjustment expense reserves, December 31	23,818,328	16,835,442
Reinsurance recoverables	<u>8,104,202</u>	<u>8,702,759</u>
Gross loss and loss adjustment expense reserves, December 31	<u>\$ 31,922,530</u>	<u>\$ 25,538,201</u>

As a result of changes in estimates of insured events in prior years, the loss and loss adjustment expense reserves decreased by \$2,063,193 and \$3,143,030 in 2002 and 2001, respectively. In evaluating its 2002 and 2001 actuarial reports, the Company determined that the actual experience in its general liability and auto liability business has developed more favorably than original estimates. As a result, management has determined that the reserve reduction for prior years is appropriate.

6. SUBORDINATED DEBT

In September 2001, NIAC repaid the remaining principle of the subordinated debt.

In 1989, a total of \$1,300,000 was provided by foundations to NIAC in the form of restricted assets in the amounts listed below:

The Ford Foundation	\$ 500,000
Wallace Alexander Gerbode Foundation	250,000
David and Lucile Packard Foundation	250,000
San Francisco Foundation	100,000
Marin Community Foundation	100,000
Walter S. Johnson Foundation	100,000
	<hr/>
Total	\$ 1,300,000

NIAC paid 2% simple interest per year on these funds. Payment of interest was made in quarterly installments and amounted to \$2,334 in 2001.

Principal amounts were considered to be due and payable only when an independent actuary certified that to make such repayment would in no way jeopardize the financial stability of NIAC. Interest payments were able to be postponed at any time if management determined that paying interest would jeopardize the financial stability of NIAC.

Prior to 2001, NIAC repaid \$1,144,400 of the subordinated loans. In March 2001, NIAC's independent actuary concluded that NIAC could repay the remaining \$155,600 principal in fiscal year 2001 without jeopardizing NIAC's ability to grow. Upon repayment of the subordinated debt the investment balances became unrestricted.

7. LOAN PAYABLE

On May 1, 2000, NIAC entered into an agreement with the California Statewide Communities Development Authority (the "Authority") to borrow \$4,560,000, which represents all of the proceeds from the Authority's May 1, 2000, Series 2000A bond issuance.

Interest payments are due monthly. The interest rate is variable, dependent upon the current market rate as determined by an independent marketing agent named in the original agreement. The interest rate is assessed on a weekly basis.

Principal repayments are due annually on September 1, as follows:

2003	\$ 165,000
2004	170,000
2005	180,000
2006	185,000
2007	195,000
Thereafter	3,345,734
	<hr/>
Total	\$ 4,240,734

The bond proceeds were used to finance the costs of the acquisition, construction, improvement and equipping of NIAC's new administrative building. As of December 31, 2002, NIAC had no unspent loan proceeds.

Interest expense on the bonds totaled \$106,328 and \$119,563 for the years ended December 31, 2002 and 2001, respectively. Interest expense incurred from May 1, 2000 through March 1, 2001 has been capitalized as part of the building. Capitalized interest to March 1, 2001 was \$127,296.

8. REINSURANCE

Effective January 1, 2001, NANI provides reinsurance to affiliates in the Group. In the normal course of business, NANI reinsures with other third-party reinsurers through contractual agreements. The reinsurers are rated A++ by A.M. Best. Such agreements serve to limit the ceding companies' loss on large claims. Risks reinsured would become an expense of the ceding companies in the event the reinsurer is unable to or will not fulfill the obligations assumed under the agreements.

For 2002 and 2001, NIAC obtained reinsurance coverage from NANI of \$850,000 excess of a company retention of \$150,000 and aggregate cover of \$2 million excess of \$1 million. For 2002 and 2001, ANI-RRG obtained reinsurance coverage from NANI of \$975,000 excess of a company retention of \$25,000 and aggregate cover of \$2 million excess of \$1 million. In addition NIAC and ANI-RRG offer umbrella coverage. These policies are ceded 100% on a treaty basis. NANI retrocedes to a third party reinsurer as follows:

	2002	2001
First Excess of Loss	\$250,000 - \$1,000,000	\$250,000 - \$1,000,000
Aggregate Excess of Loss	\$1,000,000 - \$3,000,000	\$1,000,000 - \$3,000,000
Umbrella 97.5% Quota Share	\$1,000,000 - \$10,000,000	\$1,000,000 - \$10,000,000

These limits are on a "per occurrence" basis and "losses" for the purposes of these agreements include indemnity and allocated loss adjustment expenses.

Before January 1, 2001, NIAC maintained similar reinsurance coverages with third-party companies.

The table below reflects the financial statement captions which are stated net of the effects of reinsurance:

<i>Reinsurance ceded</i>	2002	2001
Premium earned	\$ 4,445,141	\$ 3,526,937
Loss and loss adjustment expenses incurred	1,151,159	4,200,410

For the years ended December 31, 2002 and 2001 NANI received ceding commission of \$885,064 and \$425,458, respectively. The ceding commission is recorded as a reduction of commission expense.

In 1994 - 1996, for the first layer of reinsurance, NIAC paid a provisional reinsurance premium based on gross premiums written, subject to additional premium in the event of unfavorable loss experience. Considerable judgment is involved in estimating the ultimate premium to be paid under this reinsurance agreement. NIAC accrues additional premium based on expected loss experience.

In 1997 - 2000 NIAC participated in a profit-sharing provision in the first layer of reinsurance. Based on expected loss experience NIAC has accrued provisional profit sharing payments received as a liability in its financial statements.

In 1994 - 1996, for the second layer, NIAC paid a fixed reinsurance premium based on gross premiums written, subject to a profit-sharing arrangement which could result in a refund of reinsurance premium as a result of favorable loss experience. As a result of experience to date, no provision has been made for potential profit sharing under this agreement.

For 1997 - 2000 for the second layer, NIAC pays a fixed reinsurance premium based on gross premiums written.

For 1994 - 2000, for the third layer, NIAC paid a fixed reinsurance premium based on gross premiums written.

Reinsurance recoverables at December 31, 2002 and 2001 are due from two third-party reinsurance companies, both of which are rated A++ by A.M. Best.

9. 401(k) PROFIT SHARING PLAN

As of January 1, 1999, NIAC adopted a new safe harbor 401(k) plan (the "Plan"). The employer contributions are limited to 4% of each employee's gross salary. Eligibility for the plan occurs on the first day of each quarter. On January 1, 2001, the Plan was transferred to AMS. The amounts contributed to the Plan were \$107,536 and \$90,114 in 2002 and 2001 respectively.

10. CAPITAL AND SURPLUS

ANI-RRG and NANI are required by the Vermont Department of Banking, Insurance, Securities, and Health Care Administration to maintain capital and surplus at minimum of \$500,000 and \$750,000, respectively. Their ability to pay dividends to their members is restricted and subject to regulatory approval. At December 31, 2002, the reported capital of ANI-RRG and NANI was in excess of the minimum regulatory requirement.

Individual audited financials for Nonprofits' Insurance Alliance of California (NLAC) and Alliance of Nonprofits for Insurance, Risk Retention Group (ANI-RRG) are available on the web at www.InsuranceforNonprofits.org, or you may request a copy to be mailed to you by calling 1-800-359-6422.