

FARM INSURANCE CORPORATION OF  
PUERTO RICO  
(a component unit of the Government of Puerto Rico)

INDEPENDENT AUDITORS' REPORT AND  
FINANCIAL STATEMENTS

JUNE 30, 2011

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditors' Report	1-2
Management's Discussion and Analysis	3-6
Financial Statements	
Statement of Net Assets	7
Statement of Revenues, Expenses and Changes in Net Assets	8
Statement of Cash Flows	9
Notes to Financial Statements	10-20

# VALDES, GARCIA , MARIN & MARTINEZ, LLP

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS  
MEMBER OF THE AICPA PRIVATE COMPANIES PRACTICE SECTION

P.O. Box 364831  
SAN JUAN, P.R. 00936-4831

TELEPHONE: (787) 725-1600  
TELEFAX: (787) 721-2795

Board of Directors  
Farm Insurance Corporation of  
Puerto Rico

## INDEPENDENT AUDITORS' REPORT

We have audited the accompanying statement of net assets of the Farm Insurance Corporation of Puerto Rico (the Corporation) (a component unit of the Government of Puerto Rico) as of June 30, 2011 and the related statements of revenues, expenses and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the accompanying financial statements present only the Farm Insurance Corporation of Puerto Rico, and are not intended to present the financial position of the Department of Agriculture of the Government of Puerto Rico, and the results of its operations and the cash flows of its property fund types and trust funds in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Farm Insurance Corporation of Puerto Rico as of June 30, 2011 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The attached Management's Discussion and Analysis on pages 3-6 is not a required part of the basic financial statements but it is supplementary information required by the Governmental Accounting Standard Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

*Valdés, García, Marín & Martínez, LLP*

San Juan, Puerto Rico  
October 31, 2011

Stamp 2622013 was affixed  
to the original.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

**FARM INSURANCE CORPORATION OF PUERTO RICO**  
**(A COMPONENT UNIT OF THE GOVERNMENT OF PUERTO RICO)**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE**  
**FARM INSURANCE CORPORATION OF PUERTO RICO**

This section of the Farm Insurance Corporation of Puerto Rico (the Corporation's) annual financial report presents our discussion and analysis of the Corporation's financial performance during the fiscal year ended on June 30, 2011. The Corporation's financial performance is discussed and analyzed within the context of the accompanying financial statements and disclosures following this section.

**Financial Highlights**

Management's Discussions and Analysis introduce the Corporation's financial statements. Financial reporting at this level uses a perspective similar to that found in the private sector which is the basis in full accrual basis of accounting.

Among the most significant financial aspects observed this year are the following:

1. The Corporation assets exceeded its liabilities by \$10,778,450, (net assets) for the fiscal year reported. In the previous year, assets exceeded liabilities by \$ 11,392,831.
2. Premiums written this year decreased in relation to previous year. For fiscal year 2010-2011 written premiums amounted to \$5,735,146 compared to \$ 6,401,147 in fiscal year 2009-2010.
3. At the date of the Financial Statements the Farm Insurance Corporation has a Waiver to insure Hydroponics and Ornamental Plantation Structures for a revision on rates.

**Overview of the Financial Statements**

This annual report consists of two parts: the Management's Discussion and Analysis and the Basic Financial Statements. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The first of the basic financial statements is the Statement of Net Assets. This is the Corporation's statement of financial position presenting information about the Corporation's overall status.

The increase or decrease in net assets may serve as a useful indicator of whether the financial position of the Corporation is improving or deteriorating. The second of the basic financial statements is the Statement of Revenues, Expenses and Changes in Net Assets. This is the operating statement of the Corporation, which reports the operating and non-operating revenues, expenses and the change in the net assets.

Both statements distinguish the activities assigned by law for which the Corporation was created. These activities are principally supported by selling of insurance to farmers and income from the Federal Crop Insurance Corporation. Evaluation of the overall health of the Corporation would extend to other non-financial factors, such as the changes in the insurance industry and occurrence of natural disasters in addition to the financial information provided in this report.

**Farm Insurance Corporation of Puerto Rico**  
**Management's Discussion and Analysis**

**Notes to financial statements**

The accompanying notes to financial statements provide information essential to a full understanding of the basic financial statements. The notes to the financial statements begin on page ten on this report.

**Financial Analysis of the Administration**

The following table provides a summary of the Corporation's net assets:

<b>Summary of Net Assets</b>			
	June 30		
	2011	2010	Net Change
Current Assets	\$ 17,946,512	\$ 17,312,222	\$ 634,290
Non Current Assets	5,098,387	5,459,991	(361,604)
Capital Assets	188,904	222,618	(33,714)
<b>Total Assets</b>	<b>\$ 23,233,803</b>	<b>\$ 22,994,831</b>	<b>\$ 238,972</b>
Current Liabilities	\$ 6,795,349	\$ 5,670,681	\$ 1,124,668
Non Current Liabilities	5,660,004	5,931,319	(271,315)
<b>Total Liabilities</b>	<b>\$ 12,455,353</b>	<b>\$ 11,602,000</b>	<b>\$ 853,353</b>
<b>Net Assets:</b>			
Invested in Capital Assets net of Related debt	\$ 188,904	\$ 222,618	\$ (33,714)
Unrestricted	10,589,546	11,170,213	(580,667)
<b>Total Net Assets</b>	<b>\$ 10,778,450</b>	<b>\$ 11,392,831</b>	<b>\$ (614,381)</b>

**Analysis as of June 30, 2011**

Fiscal year 2011 reflects an increase in total assets amounting to \$238,972, a decrease in total liabilities of \$853,353 and a decrease in total net assets of \$614,381 when compared with fiscal year 2010. Current assets increased due mainly to increase in cash of \$634,290. Non-current assets decreased mainly due to the collection of the accounts receivable from ASDA during the year. Capital assets decreased for the depreciation expense for the year. Liabilities increased due to the unearned premiums adjustment recorded during this fiscal year and the increase in unpaid claims and accounts payable to FCIC and others.

**Farm Insurance Corporation of Puerto Rico**  
**Management's Discussion and Analysis**

The following table provides a summary of the Corporation's revenues, expenses and change in net assets:

Summary of Revenues, Expenses and Changes in Net Assets  
For the years ended on June 30,

	2011	2010	Net Change
Operating Revenues	\$ 3,089,508	\$ 2,798,351	\$ 291,157
Operating Expenses	(3,964,050)	(1,981,231)	(2,072,819)
Operating Income/(Loss)	(874,542)	907,120	(1,781,662)
Non Operating Revenues	260,161	181,599	78,562
Change in Net Assets	(614,381)	1,088,719	(1,703,100)
Net assets – Beginning of year	11,392,831	10,304,112	1,088,719
Net assets – end of year	\$ 10,778,450	\$ 11,392,831	\$ (614,381)

Fiscal year 2011 reflects a decrease in total revenue and an increase in expenses. Premiums written decreased due to the migration of farmers to catastrophic insurance policies that carry a lower premium. Claims expenses increased due to storms and atmospheric events and floods that occurred during the fiscal year 2011. The Corporation had a change in net assets of \$(614,381).

**Capital Assets**

The Corporation's investment in capital assets, net of accumulated depreciation as of June 30, 2011 and 2010, was \$ 188,904 and \$ 222,618, respectively. The total net decrease in the net capital assets investment was 15% (including the depreciation expense of \$60,422).

Capital Assets  
For the years ended on June 30,

	2011	2010	Net Change
Equipment	\$ 731,945	\$ 706,451	\$ 25,494
Vehicles	77,743	77,743	-
	809,688	784,194	25,494
Less: Accumulated Depreciation	(620,784)	(561,576)	(59,208)
Change in Net Assets	188,904	222,618	(33,714)



**Farm Insurance Corporation of Puerto Rico**  
**Management's Discussion and Analysis**

**Line of Credit**

During the fiscal year ended June 30, 2005 the Corporation borrowed \$6,500,000 from FIDA under a non-revolving credit line for working capital purposes. The line of credit bears annual interest at 2.25% over LIBOR rate. As of June 30, 2011 the outstanding balance amounted \$5,660,004 and \$5,931,319 as of June 30, 2010. During the fiscal year 2010-2011 the Corporation paid principal amounting to \$271,315.

The Corporation is obligated to pay FIDA the outstanding balance of the line of credit after ASDA has paid its debts to the Corporation.

On February 9, 2006 FIDA, through resolution No. 2005-07, modified the terms of the line of credit due to the cash flow problems experienced by the Corporation. FIDA has agreed to accept a cash payment of the principal balance at no interest nor penalties, after ASDA has paid its debts to the Corporation.

**Subsequent Events**

In August 2011, Hurricane Irene affected Puerto Rico. As a result of said atmospheric event, the Corporation received 2,924 claims from farmers. Claims for losses included all kinds of crops and plantations under insurance policies issued by the Corporation from the regional areas.

Estimated losses on claims filed by the farmers amount to approximately \$4,000,000.

In October 2011, the Insurance Commissioner Office of the Government of Puerto Rico conducted an evaluation with the purpose of determining the amount of the maximum loss obligations that the Corporation may contract for the fiscal year 2011-2012. As a result of the evaluation, the Insurance Commissioner Office recommended the Corporation to establish and separate a reserve not less than \$10,592,570 to cover the maximum estimated loss exposure for the next fiscal year.

**Contacting the Corporation's Financial Management**

This financial report is designed to provide a general overview of the Corporation's finances, and to demonstrate the Corporation's commitment to public accountability. If you have any questions about this report or you would like to request additional information, please contact the Corporation's Finance Department at (787) 722-2748.

FINANCIAL STATEMENTS .

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

STATEMENT OF NET ASSETS

JUNE 30, 2011

ASSETS

CURRENT ASSETS

Cash and cash equivalents	\$ 12,395,742
Accounts receivable, net	5,314,355
Prepaid expenses	<u>236,415</u>

Total current assets 17,946,512

NON-CURRENT ASSETS

Accounts receivable, net	5,098,387
Capital assets, net	<u>188,904</u>

Total non-current assets 5,287,291

Total assets \$ 23,233,803

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES

Unpaid claims	\$ 93,615
Accounts payable	
Federal Crop Insurance Corporation	1,249,088
Other	261,182
Accrued expenses	706,498
Unearned premiums	<u>4,484,966</u>

Total current liabilities 6,795,349

NON-CURRENT LIABILITY

Line of credit	<u>5,660,004</u>
----------------	------------------

Total liabilities 12,455,353

COMMITMENTS

-

NET ASSETS

Invested in capital assets	188,904
Unrestricted	<u>10,589,546</u>

Total net assets 10,778,450

Total liabilities and net assets \$ 23,233,803

See accompanying notes to financial statements.

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

FOR THE YEAR ENDED JUNE 30, 2011

Operating revenues		
Premiums written		\$ 5,735,146
Ceded premiums		<u>(2,767,181)</u>
Net premiums		2,967,965
Commissions revenue		95,996
Other revenue		<u>25,547</u>
Total operating revenues		<u>3,089,508</u>
Operating expenses		
Claims		2,127,544
Salaries and employee benefits		2,024,093
Insurance		99,180
Rent		143,583
Professional services		469,962
Depreciation		60,422
Other		<u>193,024</u>
Total operating expenses		5,117,808
Reimbursement of administrative and operating expenses		<u>(1,153,758)</u>
Net operating expenses		<u>3,964,050</u>
Operating loss		(874,542)
Non-operating revenue - interest		<u>260,161</u>
Change in net assets		(614,381)
Net assets at beginning of year		<u>11,392,831</u>
Net assets at end of year		<u>\$ 10,778,450</u>

See accompanying notes to financial statements.

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2011

Cash flows from operating activities:	
Receipts from customers (net of reinsurance)	\$ 4,055,246
Commissions and other revenue	35,984
Salaries and employee benefits paid	(2,029,971)
Claims paid and payments to suppliers	<u>(1,832,259)</u>
Net cash provided by operating activities	<u>229,000</u>
Cash flows from capital and related financing activities:	
Purchase of capital assets	(26,708)
Payments of line of credit	<u>(271,315)</u>
Net cash used in capital and related financing activities	<u>(298,023)</u>
Cash flows from and net cash provided by investing activity:	
Interest received	<u>260,161</u>
Net increase in cash and cash equivalents	191,138
Cash and cash equivalents at beginning of year	<u>12,204,604</u>
Cash and cash equivalents at end of year	<u>\$12,395,742</u>
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	\$ (874,542)
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Depreciation	60,422
Change in assets and liabilities	
(Increase) decrease in:	
Accounts receivable	18,019
Prepaid expenses	(99,565)
Increase (decrease) in:	
Accounts payable and unpaid claims	1,300,596
Accrued expenses	(5,878)
Unearned premiums	<u>(170,052)</u>
Net cash provided by operating activities	<u>\$ 229,000</u>

See accompanying notes to financial statements.

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and reporting entity

The Farm Insurance Corporation of Puerto Rico (the Corporation) is an instrumentality of the Government of Puerto Rico ascribed to the Department of Agriculture (the Department). As a component unit of the Department, the Corporation is also included as part of the Department's reporting entity.

The Corporation was created by Act Number 166 (the Act) of August 11, 1988 to provide insurance to farmers against losses or damages to plantations, crops, animals, birds, and others caused by natural disasters. The Corporation is responsible for its debts and is entitled to surpluses. The Commissioner of Insurance of Puerto Rico has the authority to evaluate accrued reserves in order to determine their adequacy and to make recommendations.

The Board of Directors is composed of five members including, the Secretary of the Department of Agriculture (as President), the Dean of the Agricultural Sciences Faculty of the Mayaguez Campus of the University of Puerto Rico, a representative of the Government Development Bank for Puerto Rico and two bonafide farmers appointed by the Governor with the consent of the Senate of Puerto Rico.

The Board of Directors appoints the Executive Director of the Corporation, who is responsible for the direct administration of the Corporation in accordance with the policies and procedures established by the Board of Directors.

Basis of presentation

The Corporation's financial statements are presented as an enterprise fund and conform to the provisions of Governmental Accounting Standards Board Statement No. 34 ("GASB 34") "Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments." GASB 34, as amended, establishes standards for external financial reporting for all state and local governmental entities, which includes a statement of net assets, a statement of revenues, expenses and changes in net assets and a statement of cash flows. It requires the classification of net assets into three components: invested in capital assets - net of related debt, restricted, and unrestricted.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

These classifications are defined as follows:

- Invested in capital assets - net of related debt - Consist of capital assets, net of accumulated depreciation and reduced by the outstanding balance of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.
- Restricted net assets - Consist of constraints placed on net assets use through external constraints imposed by creditors (such as through covenants), contributors, or law or regulations of other governments or constraints imposed by law through constitutional provision or enabling legislation.
- Unrestricted net assets - Consist of all other assets that do not meet the definitions of "restricted" or "invested in capital assets - net of related debt".

As allowed by Governmental Accounting Standards Board ("GASB") Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and other Governmental Entities that use Proprietary Fund Accounting", the Corporation has elected not to apply all Financial Accounting Standards Board Statements and Interpretations, issued after November 30, 1989.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting

The accrual basis of accounting is used by the Corporation. Under the accrual basis, revenues are recognized when earned and expenses are recorded as liabilities when incurred, without regard to receipt or payment of cash.

Earned premiums

Insurance premiums are recognized as income during the period covered by the policies issued to the farmers. The insurance policies period cover from April 1<sup>st</sup> to March 31<sup>st</sup>. The portion corresponding to the next fiscal year is deferred and recognized as earned during that year.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Unbilled receivables

Unbilled receivables represent management's estimate of the unearned premiums related to the unwritten insurance policies for the period that covers from April 1, 2011 to March 31, 2012.

Unpaid claims

The liability for unpaid claims consists of the estimated amount of the probable claims of the farmers. The Corporation's management believes that the liability for unpaid claims is adequate to cover the ultimate net costs of losses and claims as of year-end. However, the liability is necessarily based on estimates and no representation is made that the amounts ultimately paid may not be more or less than such estimates as of year-end.

Cash equivalents

The Corporation classifies as cash equivalents the certificates of deposits purchased with original maturities of ninety days or less.

Capital assets

The Corporation's capital assets are recorded at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the assets. The Corporation recognizes as capital assets those assets that have an unitary cost of \$500 or more. The estimated useful lives of capital assets are as follows:

Motor vehicles	5 years
Computer equipment	5 years
Office furniture and equipment	5 to 10 years
Other equipment	5 to 10 years

Compensated absences

The vacation policy of the Corporation generally provides for the accumulation of thirty (30) days of vacation and eighteen (18) days of sick leave annually. Vacation time is fully vested to the employees from the first day of work. In the event of resignation, an employee is reimbursed for accumulated vacation days up to the maximum allowed of sixty (60) days. Separation of employment prior to the use of all or part of the sick leave terminates all rights for compensation except that, in the event of retirement and having more than ten years of continued services, an employee is reimbursed for accumulated sick leave days up to the maximum allowed of ninety (90) days.

(Continues)



FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated absences, such as unpaid vacation and sick leave pay, are accrued when incurred using the pay of salary rates in effect at the statement of net assets date. An additional amount is accrued for certain salary related benefits associated with the payment of compensated absences.

As per Law Number 156 of August 20, 1996, for the current fiscal year, the employees have the right to accumulate the excess of 60 and 90 days in vacation and sick leave, respectively, until December 31<sup>st</sup> of each year. The excess should be paid to the employees before March 31<sup>st</sup> of the following year.

Accounting for pension costs

The management of the Corporation accounts for pension costs in accordance with the provisions of Governmental Accounting Standards Board ("GASB") Statement No. 27 "Accounting for Pensions by State and Local Governmental Employers".

GASB No. 27 establishes standards of accounting and financial reporting for pension expenditures/expenses and related pension liabilities, pension assets, note disclosures, and required supplementary information in the financial reports of state and local governmental employers.

The statement defines that the pension expense is equal to the statutory required contribution to the employees' retirement system. A pension liability or asset is reported equal to the cumulative difference between statutory required and actual contributions.

Statement of cash flows

The accompanying statement of cash flows is presented in accordance with the provisions of GASB Statement No. 9, as amended, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting". For purposes of reporting cash flows, cash includes cash on hand, amounts due from banks, and items in process of collection.

Operating revenues and expenses

Operating revenues and expenses arise from the sale of insurance to farmers and the services provided to them as well as all revenues and expenses not related to capital and related financing activities.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Risk management

The Corporation is exposed to various risks of loss from torts, theft of, damage to, and destruction of assets, business interruption, errors and omissions, employee injuries and illnesses, natural disasters and other losses. Commercial insurance coverage is obtained for claims arising from such matters. The commercial insurance coverage is negotiated by the Department of Treasury of the Government of Puerto Rico and the cost is paid by the Corporation.

Future adoption of accounting pronouncements

The GASB has issued the following statements, which the Corporation has not yet adopted:

	<u>Statement</u>	<u>To be adopted in Fiscal year ended</u>
57	OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans	June 30, 2012
61	The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and No. 34	June 30, 2013
62	Codification of Accounting and Financial Reporting Guidance Contained in Pre - November 30, 1989 FASB and AICPA Pronouncements	June 30, 2013
63	Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position	June 30, 2013

The Corporation's management has concluded that the adoption of these statements will not have a significant impact on the Corporation's financial statements.

NOTE 2 CUSTODIAL CREDIT RISK - DEPOSITS

Custodial credit risk is the risk that, in the event of a bank failure, the Corporation's deposits might not be recovered. The Corporation maintains all cash deposits in commercial banks located in Puerto Rico.

Under the Government of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of Treasury of Puerto Rico in the Corporation's name. At year-end the Corporation's bank balance in commercial banks amounts to \$12,520,258.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 2 CUSTODIAL CREDIT RISK - DEPOSITS (CONTINUED)

The Corporation established, in accordance with the requirements of the Federal Crop Insurance Corporation (FCIC), separate bank accounts dedicated solely to the federally reinsured crop insurance program. For the fiscal year ended June 30, 2011 the Corporation deposits all producer-paid premium, reinsurance recoveries, and FCIC paid premium subsidy in the accounts and pays all crop insurance losses and reinsurance premium from the accounts. Additionally, the Corporation must not commingle other funds not related to the federal crop insurance program.

NOTE 3 ACCOUNTS RECEIVABLE - NET

The net accounts receivable of the Corporation as of June 30, 2011 are composed of the following:

Accounts receivable

Agricultural Services and Development Administration	\$ 5,215,440
Unbilled receivables	
Agricultural Services and Development Administration	1,923,956
Federal Crop Insurance Corporation	3,104,591
Other	<u>247,546</u>
	10,491,533
Less: allowance for uncollectible amounts	<u>78,791</u>
	10,412,742
Less: current accounts receivable, net	<u>5,314,355</u>
Non-current accounts receivable, net	<u>\$ 5,098,387</u>

The accounts receivable from the Agricultural Services and Development Administration (ASDA), another instrumentality ascribed to the Department, mainly include insurance premiums of policies issued to farmers for which ASDA has agreed to pay the Corporation. The above aggregate receivable balances have been classified as noncurrent because they are not expected to be collected within one year from the statement of net assets date, June 30, 2011. The unbilled receivable represents management's estimate of the unearned premiums related to unwritten insurance policies for the period that covers from April 1, 2011 to March 31, 2012.

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 4 CAPITAL ASSETS - NET

Capital assets as of June 30, 2011 consist of the following:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Capital assets being depreciated:				
Equipment	\$706,451	\$26,708	\$(1,214)	\$731,945
Motor vehicles	<u>77,743</u>	<u>-</u>	<u>-</u>	<u>77,743</u>
	<u>784,194</u>	<u>26,708</u>	<u>(1,214)</u>	<u>809,688</u>
Less accumulated depreciation:				
Equipment	(483,833)	(60,422)	1,214	(543,041)
Motor vehicles	<u>(77,743)</u>	<u>-</u>	<u>-</u>	<u>(77,743)</u>
	<u>(561,576)</u>	<u>(60,422)</u>	<u>1,214</u>	<u>(620,784)</u>
Capital assets, net	<u>\$222,618</u>	<u>\$(33,714)</u>	<u>\$ -</u>	<u>\$188,904</u>

NOTE 5 PENSION PLAN

The employees of the Farm Insurance Corporation of Puerto Rico participate in the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (the "System"). The System is a defined benefit, cost-sharing, multi-employer plan sponsored by the Government under the terms of Act No. 447 of 1951, as amended. Participation is mandatory for regular employees. The System issues a publicly available financial report that includes its financial statements and required supplementary information.

Members who have attained at least 55 years of age and have completed at least 30 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life.

The amount of the annuity shall be 1.5% of the average compensation multiplied by the number of years of creditable service up to 20 years, plus 2% of the average compensation multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$300 per month.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 5 PENSION PLAN (CONTINUED)

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive up to a maximum of 65% of the average compensation or, if they have attained 55 years of age, will receive up to a maximum of 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability up to a maximum benefit of 50% of the average compensation. However, for non-occupational disability, a member must have at least 10 years of creditable service.

Act No. 1 of 1990 made certain amendments applicable to new participants joining the System effective April 1, 1990. These changes consist principally of the establishment of contributions at 8.275% of their monthly gross salary, an increase in the retirement age to 65, a decrease in the annuity benefit to 1.5% of the average compensation for all years of creditable service, a decrease in the maximum disability, and death benefits annuities from 50% to 40% of average compensation, and the elimination of the Merit Annuity for participants who have completed 30 years of creditable service.

The contribution requirements for both employees and employers are established by law and are not actuarially determined. Employees are required to contribute 5.775% or 8.275% of their monthly gross salary. The Corporation is required to contribute 9.275% of its employees' gross salaries.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the System, was enacted with the purpose of establishing a new pension system ("System 2000"). System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, had the option to either stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000, are the only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as cash balance plan. Under this new plan, there is a pool of pension assets, which are invested by the System, together with those of the current defined benefit plan. Benefits at retirement age are not guaranteed by the Government or the Corporation. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two year Constant Maturity U.S. Treasury Note; or (2) earn a rate equal to 75 percent of the return of the System 2000's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 5 PENSION PLAN (CONTINUED)

Disability pensions are not being granted under System 2000. The employer's contributions (9.275% of the employee's salary which is applicable to the Corporation) will be used to fund the current plan.

System 2000 reduced the retirement age from 65 years to 60 years for those employees who joined the current plan on or after January 1, 2000.

Funding policy

Contribution requirements are established by law and are as follows:

Corporation	9.275% of gross salary
Employees:	
Hired on or before March 31, 1990	5.775% of gross salary up to \$6,600
	8.275% of gross salary over \$6,600
Hired on or after April 1, 1990	8.275% of gross salary

Total employee contributions for the year ended June 30, 2011 amounted to approximately \$124,200.

The Corporation's contractually required contributions for the year ended June 30, 2011 amounted to approximately \$139,000. The percentage of the Corporation's required contributions were equal to the ones actually made to the System for the year ended June 30, 2011.

Additional information on the System is provided in its financial statements for the year ended June 30, 2011, a copy of which can be obtained from the Employees' Retirement System of the Government of Puerto Rico and its instrumentalities, PO Box 42003, San Juan, Puerto Rico 00940-2003.

NOTE 6 REINSURANCE

Federal Crop Insurance Corporation Reinsurance

In the ordinary course of business, the Corporation cedes business to the Federal Crop Insurance Corporation (FCIC) under a contract. The existence of such reinsurance does not discharge the Corporation from its primary liability to its policyholders and, to the extent that the reinsurer is unable to meet its obligations, the Corporation would become liable.

(Continues)

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 6 REINSURANCE (CONTINUED)

At present, the Corporation maintains a reinsurance contract with the FCIC, which covers crops and plantations, but not poultry house, pineapple and equipment. The FCIC will indemnify the Corporation with respect to loss occurrences under policies of crop reinsured and will pay the Corporation in accordance with the terms specified in the reinsurance agreement.

The contract specifies that ceded premiums will be approximately 20% of the annual net book premiums, as defined by the reinsurance agreement. In addition, the FCIC paid 24.5% as expenses reimbursement based on the net book premiums of buy-up policies, as defined by the reinsurance agreement.

The Corporation agreed with the FCIC to include a policy called "Catastrophic Risk Protection Plan" (CAT). CAT is eligible crop insurance contract that provides the lowest level of coverage required to be eligible for other agricultural program benefits as specified in the Federal Crop Insurance Act (7.U.S.C. 1501 et. seq.) The FCIC will subsidize 100% of the CAT policy.

The Corporation agreed to collect an administrative fee of \$300 from policyholders for the processing expenses on a per crop and agricultural region basis, and \$30 per crop processing fee for additional coverage.

Other reinsurance

The Corporation has a reinsurance agreement with Cooperativa de Seguros Multiples de Puerto Rico which covers from June 23, 2010 through June 23, 2011. This agreement covers risks associated with poultry, ornamental and hydroponic structures. This contract does not discharge the Corporation from its primary liability to its policyholders and, to the extent that the reinsurer is unable to meet its obligations, the Corporation would become liable.

NOTE 7 UNPAID ESTIMATED CLAIMS EXPENSE

Management estimated its liability for unpaid claims to farmers as of June 30, 2011 in the amount of \$93,615 substantially related to losses caused by prior year claims.

Activity in the liability for unpaid claims and claims expense is summarized as follows:

<u>Beginning Balance</u>	<u>Incurred Claims</u>	<u>Claims Paid</u>	<u>Ending Balance</u>
<u>\$77,329</u>	<u>\$2,127,544</u>	<u>\$2,111,258</u>	<u>\$93,615</u>

FARM INSURANCE CORPORATION OF PUERTO RICO  
(a component unit of the Government of Puerto Rico)

NOTES TO FINANCIAL STATEMENTS

NOTE 8 LINE OF CREDIT

The Corporation borrowed in a prior year \$6,500,000 from the "Fondo Integral para el Desarrollo Agrícola de Puerto Rico Inc." (FIDA) under a non-revolving credit line for working capital purposes. The line of credit bears annual interest at 2.25% over LIBOR rate. As of June 30, 2011 the outstanding balance amounted to \$5,660,004. During the fiscal year ended June 30, 2011 the Corporation paid principal amounting to \$271,315.

The Corporation is obligated to pay FIDA the outstanding balance of the line of credit after ASDA has paid its debts to the Corporation.

On February 9, 2006 FIDA, through resolution No. 2005-07, modified the terms of the line of credit due to the cash flow problems experienced by the Corporation. FIDA has agreed to accept a cash payment of the principal balance at no interest nor penalties, after ASDA has paid its debts to the Corporation.

NOTE 9 COMMITMENT

On July 1, 2010 the Corporation entered into a two-year new lease agreement for its administrative offices and warehouse facilities with a monthly payment of \$10,313. The future minimum annual lease payments under the rental operating lease agreement for the years ending June 30, 2011 and 2012 are \$123,760 on each year. In July 2011, the Corporation cancelled the office facilities lease agreement and entered into a new lease agreement for a period of five years with monthly rental payments of \$9,524 for the first two years and \$10,257 for the remaining three years until July 2016. The Company leases other facilities in accordance with lease agreements carried on a month to month basis. The rent expense for the year ended June 30, 2011 was \$143,583.

NOTE 10 SUBSEQUENT EVENTS

Subsequent to the date of the accompanying financial statements, and as a result of the effects of Hurricane Irene in late August 2011, the Corporation has received claims from farmers for losses of all kinds of crops and plantations. The estimated losses claimed by the farmers are approximately \$4,000,000.

In October 2011, the Insurance Commissioner Office of the Government of Puerto Rico conducted an evaluation with the purpose of determining the amount of the maximum loss obligations that the Corporation may contract for the fiscal year 2011-2012. As a result of the evaluation, the Insurance Commissioner Office recommended the Corporation to establish and separate a reserve not less than \$10,592,570 to cover the maximum estimated loss exposure for the next fiscal year.