

Interpretation Key for Yellow Book

**United Contractors Insurance Company, Inc., RRR
December 31, 2005**

Page 2 - Assets

The assets section of page two represents the gross assets of the company and are pretty much self-explanatory. With regard to real estate, all real estate used by the company is bookable as an admitted asset. Under ordinary circumstances, a formal appraisal is not usually required. Typically use the historical cost of the acquisition depreciating the value of the building. The real property will always be carried as a historical cost and cannot be reappraised to increase surplus. There are restrictions which vary from state to state on property acquired for investment purposes being booked as an admitted asset.

5. Cash equivalents
 - Include government bonds or money market accounts readily convertible to cash on short notice.
6. Contract loans
 - This item rarely used.
9. Aggregate write-ins for invested assets
 - Write-ins in the context of the Yellow Book refer to miscellaneous items that are not preprinted on the form.
12. Investment income due and accrued
 - Most commonly for bonds.
13. Premium and consideration
 - 13.1 Uncollected premiums and agents' balances in course of collection
 - Refers only to uncollected premiums due from agents
 - 13.2 Deferred premiums, agents' balances and installments booked but deferred and not yet due
 - Refers to installment premiums that would be due from the company. Any premium due from a premium finance company would be carried under line 13.2
14. Reinsurance
 - 14.1 Amounts recoverable from reinsurers
 - Money owed from a reinsurer specifically for claims.
 - 14.2 Funds held by or deposited with reinsured companies
 - This would apply if you are the assuming reinsurance company. This number would refer to funds held by the fronting company in a funds withheld account which are owed to the assuming company.

- 14.3 Other amounts receivable under reinsurance contracts
 - Catch-all and could include unearned premium due back from a reinsurance company
- 15. Amounts receivable relating to uninsured plans
 - This item never comes up
- 16.1 Current federal and foreign income tax recoverable and interest thereon
 - If you overpay taxes, this is money due
- 16.2 Net deferred tax asset
 - This line accounts for the difference between tax accounting and normal insurance accounting and relates to an obligation to reduce the amount of booked losses for tax purposes. It is essentially a form of a prepay tax arising from those differences. It also relates to paying a tax on unearned premium that is not booked as income, since it has not been earned.
- 17. Guaranty funds receivable or on deposit
 - This would only apply to additional companies that have a recovery pending from guaranty funds
- 18. Electronic data processing equipment and software
 - Self-explanatory; listed based on acquisition costs less depreciation
- 19. Furniture and equipment, including health care delivery assets
 - Self-explanatory; listed based on acquisition costs less depreciation
- 20. Net adjustment in assets and liabilities due to foreign exchange rates
 - Self-explanatory
- 21. Receivables from parent, subsidiaries and affiliates
 - Self-explanatory
- 22. Health care and other amounts receivable
 - Self-explanatory
- 23. Aggregate write-ins for other than invested assets
 - Self-explanatory
- 24. Total assets excluding Separate Accounts, Segregated Accounts and Protected Cell Accounts
 - Self-explanatory
- 25. From Separate Accounts, Segregated Accounts and Protected Cell Accounts

- Relates to life insurance companies that have segregated accounts and/or a captive that has separate segregated cells and may be required to list the assets in the segregated cell accounts

Page 2 - Details of Write-Ins

This would be the section where you provide a greater explanation for lines 9 and 23.

Lines 2301 to 2398

This is where GAAP accounting has an advantage over SAP accounting. This advantage only applies at Line 2301.

2301 Deferred acquisition costs

- This refers to money we have paid to brokers, since the brokers get paid in advance, and yet we have not earned all of the premium associated with the commission. Under SAP accounting, we are required to write off the acquisition cost (broker fee) in the quarter it is paid, whereas under GAAP accounting, we can treat the deferred acquisition cost (commission on unearned premium) as an asset.

2302 Refers to prepaid reinsurance and unearned premium.

- Although there is no particular advantage over GAAP accounting verse SAP accounting, in GAAP accounting, we gross it up, and in SAP accounting you show your unearned premium net of reinsurance. In either way the bottom line comes out the same.

2303 Money paid in advance to your claims adjusting company

2398 Summary of remaining write-ins for Line 23 of overflow page

- There simply is not enough room to list the information here in detail. (See page 108P, called an Overflow Page; this provides the necessary detail). Again, this is a function of grossing up the reinsurance numbers on a GAAP basis and netting the numbers on a SAP basis to get to the bottom line number.

Page 3 - Liabilities, Surplus and Other Funds

1. Losses

- Includes only unpaid reserves and IBNR; does not include reserved and IBNR loss costs adjustment expenses. For companies filing on a GAAP basis, this line is gross of reinsurance. See page 2, line 2398

2. Reinsurance payable on paid losses and loss adjustment expenses

- This only applies to an assuming reinsurance company and only refers to money owed from the reinsurance company to the primary company for losses actually paid

3. Loss adjustment expenses

- This includes reserved but unpaid loss costs adjustment expenses as well as LAE on IBNR

4. Commissions payable, contingent commissions and other similar charges
 - This refers typically to commissions owed brokers on direct bill accounts
5. Other expenses (excluding taxes, licenses and fees)
 - Self-explanatory
6. Taxes, licenses and fees (excluding federal and foreign income taxes)
 - Relates to unpaid premium taxes
- 7.1 Current federal and foreign income taxes
 - Refers to unpaid federal taxes for accrued taxable income
- 7.2 Net deferred tax liability
 - This item relates to the timing differences between book accounting and tax accounting. If the liabilities exceeded the assets on Line 16.2 of page 2, then the number would be placed on this line
8. Borrowed money and interest thereon
 - Standard loan, not including a surplus note
9. Unearned premiums
 - Self-explanatory; this includes premium that has been collected but covers future portions of a policy. There is a difference in GAAP and SAP accounting. Under GAAP accounting you generally show your assets and liabilities gross of reinsurance. Under SAP accounting you show it net of reinsurance. There is no advantage between GAAP accounting and SAP accounting, it is simply a different methodology, and either way does not affect surplus
10. Advance premiums
 - This is a line that is rarely used and would apply if you were booking premiums for future effective dates
11. Dividends declared and unpaid
 - 11.1 Stockholders
 - 11.2 Policyholders
 - Self-explanatory. If the Board elects to give a dividend, it would be listed here. NOTE: UCIC does not intend to give a dividend but may redeem stock in order to give the policyholders back money. If UCIC undertook an obligation to redeem stock, it would not be listed in line 11; that obligation would be scheduled on line 28
12. Ceded reinsurance premiums payable
 - This refers to business that we have written and ceded to the reinsurer but have not yet paid the reinsurer the money. NOTE: Once the money leaves UCIC and wired to Gresham, we treat it as being paid and would not be listed on line 12
13. Funds held by company under reinsurance treaties

- This would apply to a funds withheld account where UCIC would hold onto funds under a reinsurance treaty until the premiums were earned by the reinsurer
14. Amounts withheld or retained by company for account of others
 - This is usually used for things like payroll taxes
 15. Remittances and items not allocated
 - Catch-all item; most companies use this for suspense accounts where they have collected cash, and they have not figured out how to allocate it
 16. Provision for reinsurance
 - This line would typically apply to a carrier that was using unauthorized reinsurance without the use of a funds withheld or Reg. 114 arrangement. Thus unrecognized reinsurance would have to be listed as a liability on this line. Here is another advantage of GAAP accounting over SAP accounting in that under GAAP accounting you are not required to take that penalty against your collateral
 17. Net adjustments in assets and liabilities due to foreign exchange rates
 - Self-explanatory
 18. Drafts outstanding
 - This is essentially the equivalent of outstanding checks. If you were using drafts instead of checks to pay claims, normally you would not deduct the money paid from your balance until the draft cleared. This is a line to show that outstanding liability
 19. Payable to parent, subsidiaries and affiliates
 - Self-explanatory
 20. Payable for securities
 - Self-explanatory
 21. Liability for amounts held under uninsured accident and health plans
 - Self-explanatory
 22. Capital notes and interest thereon
 - Never used
 23. Aggregate write-ins for liabilities
 - This is a catch-all for liabilities not otherwise listed above
 24. Total liabilities excluding protected cell liabilities
 - Self-explanatory
 25. Protected cell liabilities

- See line 25 of page 2 under Assets section. This offsets assets listed under protected cells and only applies if the company does have segregated and/or protected cell accounts
26. Total liabilities
- Self-explanatory
27. Aggregate write-ins for special surplus funds
- This is an item that is rarely used. Surplus note obligations are not included here, since a surplus note requires approval of the Department of Insurance. This is a rarely used catch-all for an obligation to pay back surplus funds other than under a surplus note arrangement
28. Common capital stock
- Under UCIC, this represents the collected subscription fees. Accounting may be allowed to show par value on line 28 and the excess on line 32. In any event, we would get to the same result, and it is simpler to show the full amount of the subscription fee on line 28. NOTE: The subscription fees will stay there indefinitely, even though the stock purchase technically expires three years after the termination of the policy involved unless there is an earlier redemption. The only time this line would be reduced is if we actually redeem stock or the money otherwise left the company
29. Preferred capital stock
- We do not have preferred stock
30. Aggregate write-ins for other than special surplus funds
- This is a totaling from the details listed in Items 2301 through Items 3099 below entitled, "Detail of Write-Ins"
31. Surplus notes
- Refers to a financing vehicle used by insurance companies where money is lent into surplus. The surplus note stipulates that the money will not be paid back unless allowed by the Insurance Commissioner. Even though technically this is a debt instrument, this allows you to count the funds received under the surplus note as equity
32. Gross paid in and contributed surplus
- This line item would apply to companies that only show the par value of the capital stock on line 28. This would reflect the difference between the par value of the capital stock and the cash contributed by this shareholder
33. Unassigned funds (surplus)
- Retained earnings. This represents our underwriting and investment profit after and after payment of claims, calculation of reserves and IBNR and operating expenses of the carrier (such as captive management fees and attorney fees)

34. Less treasury stock, at cost:
- 34.1 shares common
 - 34.2 shares preferred
 - This line is rarely used. This would refer to a transaction in which the company is buying back stock. If the transaction was committed to but not completed, it would be booked here. Again, this item is rarely used.
35. **Surplus as regards policyholders**
- **This is the key number to show the financial viability of the company.** Simply stated, this is the net worth of the insurance company. This represents the assets minus the liabilities. NOTE: The term “capital” of “capital and surplus” is not distinguished in line 35. An alternate way of filling out the line items would be to put surplus in line 33, and the capital would be the sum of lines 27 through 32. In any event, we do not segregate between capital and surplus and list the net worth of the company as a combined number on line 35
36. Totals
- This line is simply the totals of liabilities and surplus. This number must balance with the assets listed on line 26 of the Assets section on page 2

Page 4 - Statement of Income

Underwriting Income

1. Premiums earned – Deductions
 - This is net of reinsurance which has already been deducted
2. Losses incurred
 - This includes paid, unpaid and IBNR. This number is net of reinsurance; it does not include LAE
3. Loss expenses incurred
 - This is the LAE (Lost Adjustment Expenses)
4. Other underwriting expenses incurred
 - Normal operating expenses (not necessarily limited to underwriting). See detail on page 11, column 2. This includes acquisition costs, including broker commissions, operating expenses of the company, all commissions, normal operating expenses, such as attorney fees, captive manager fees. NOTE: The ceding commission on the reinsurance reduces this amount

5. Aggregate write-ins for underwriting deductions
 - Rarely used item.
6. Total underwriting deductions
 - Self-explanatory
7. Net income of protected cells
 - Not normally used, unless we are dealing with a captive with segregated cells
8. Net underwriting gain (loss)
 - For practical purposes, this represents your pre-tax income, except for interest income, investment income and other miscellaneous income not associated with policies written, less all expenses. This number represents profits that go into surplus. Taxes, however, have not yet been deducted before this number is plowed into the surplus. Federal income taxes of 34 percent have not been deducted from this number, however, premium taxes already have been deducted. Therefore, 66 percent of this number represents augmentation of surplus

Investment Income

9. Net investment income earned (Exhibit of Net Investment Income)
 - Self-explanatory. This will include investment and bank interest. UCIC has only been achieving bank interest. Now that the bank accounts have increased, we will be utilizing the services of an investment counselor
10. Net realized capital gains (losses) less capital gains tax
 - Self-explanatory
11. Net investment gain (loss)
 - Self-explanatory

Other Income

12. Net gain (loss) from agents' or premium balances charged off
 - Self-explanatory - Skip
13. Finance and service charges not included in premiums
 - Self-explanatory - Skip
14. Aggregate write-ins for miscellaneous income
 - Self-explanatory - Skip
15. Total other income
 - Self-explanatory - Skip

16. Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes
 - The net income number before federal taxes; represents the sum of the underwriting and investment income. See also line 18 which is the same
17. Dividends to policyholders
 - Used if dividends are declared to policyholders (Usually requires DOI approval)
18. Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes
 - This item is self-explanatory. This line is used to indicate the net income after the deduction for dividends and taxes which represent a deduction to the income before taxes and dividends
19. Federal and foreign income taxes incurred
 - Represents federal income tax liability of 34 percent
20. Net income
 - Net income after taxes. This will be the amount that will be used to augment surplus

Capital and Surplus Account

21. Surplus as regards policyholders, December 31 prior year
 - This line items lists the surplus for the previous year

Gains and (Losses) in Surplus

22. Net income
 - Self-explanatory - Skip
23. Net transfers (to) from Protected Cell accounts
 - Self-explanatory - Skip
24. Change in net unrealized capital gains or (losses) less capital gains tax
 - Self-explanatory - Skip
25. Change in net unrealized foreign exchange capital gain (loss)
 - Self-explanatory - Skip
26. Change in net deferred income tax
 - Self-explanatory - Skip

27. Change in nonadmitted assets
 - Self-explanatory - Skip
28. Change in provision for reinsurance
 - Self-explanatory - Skip
29. Change in surplus notes
 - The initial surplus note of \$600,000.00 was booked in 2005. Any additional funds received from surplus notes in any particular accounting period will be listed in line 29
30. Surplus (contributed to) withdrawn from protected cells
 - This refers to an accounting item when the insurance company has segregated cells. This typically applies to a segregated cell captive
31. Cumulative effect of changes in accounting principles
 - This would only apply if there was a change in accounting principles, like going from GAAP to statutory accounting. It is rarely used.
32. Capital changes:
 - 32.1 Paid in
 - 32.2 Transferred from surplus (Stock Dividend)
 - 32.3 Transferred to surplus
 - This represents additional paid-in capital. Line 32.1 represents subscription fees collected
33. Surplus adjustments:
 - 33.1 Paid in
 - 33.2 Transferred to capital (Stock Dividend)
 - 33.3 Transferred from capital
 - Line 33.1 represents capital contributions during the current year—generally from policyholders for their common stock. Line 33.2 would be a reduction in surplus, generally due to a shareholder dividend. Line 33.3 would be an increase in surplus other than newly contributed capital. This item is rarely used.
34. Net remittances from or (to) Home Office
 - Generally only used by US branches of alien parents when funds are transferred out of the branch to the parent.
35. Dividends to stockholders
 - Self-explanatory
36. Change in treasury stock
 - Self-explanatory

37. Aggregate write-ins for gains and losses in surplus
 - This is detail from detailed write-in sections 0501 through 3799 listed below
38. Change in surplus as regards policyholders for the year
 - Represents the increase in surplus (as regards to policyholders) for the year. For 2005, the figure represents the total amount of surplus
- 39. Surplus as regards policyholders, December 31 current year**
 - **This is a key number which reveals the amount of surplus in the company and is the major single line item factor of an insurance company's solvency**

Page 5 – Cash Flow

General Statement: The cash flow statement essentially takes the income statement and adjusts it for non-cash items to turn it into a cash flow statement. Non-cash flow items may include things like premiums earned but not collected or other obligations. On lines 1 through 4, a non-bracketed number means cash in, a bracketed number means Cash out. On lines 5 through 10, an non-bracketed figure means cash out, a bracketed number means cash in. Line 11 is therefore a positive number showing cash in.

Cash from Operations

1. Premiums collected net of reinsurance
 - This amount is normally net of reinsurance. It is the sum of the earned and unearned premiums, adjusted for uncollected premiums and unpaid reinsurance premiums. However, because page 2, line 9, is gross of reinsurance, this amount is actually a hybrid of gross and net.
2. Net investment income
 - Self-explanatory
3. Miscellaneous income
 - Self-explanatory
4. Total
 - Self-explanatory
5. Benefit and loss related payments
 - Represents the amount of paid claims and adjusting expenses, usually net of reinsurance. Similar to line 1 above, it is a hybrid of gross and net of reinsurance, because page 3, line 1, is gross of reinsurance on a GAAP basis.
6. Net transfers to Separate, Segregated Accounts and Protected Cell Accounts

- Only used by Segregated Account or Protected Cell captives, when funds are transferred out of the cell into another entity
7. Commissions, expenses paid and aggregate write-ins for deductions
 - Represents the net difference between commissions and expenses that you have paid out after converted to a cash basis
 8. Dividends paid to policyholders
 - Self-explanatory
 9. Federal and foreign income taxes paid (recovered)/net of tax on capital gains losses)
 - Self-explanatory
 10. Total
 - Self-explanatory
 11. Net cash from operations
 - Because of the distortions in line 1 and line 5, this amount is misleading. The amount on line 16.8 should be deducted to get a true cash fro operations figure.

Cash from Investments

12. Proceeds from investments sold, matured or repaid:
 - 12.1 Bonds
 - 12.2 Stocks
 - 12.3 Mortgage loans
 - 12.4 Real estate
 - 12.5 Other invested assets
 - 12.6 Net gains or (losses) on cash, cash equivalents and short-term investments
 - 12.7 Miscellaneous proceeds
 - 12.8 Total investment proceeds
 - Self-explanatory - Skip
13. Cost of investments acquired (long-term only):
 - 13.1 Bonds
 - 13.2 Stocks
 - 13.3 Mortgage loans
 - 13.4 Real estate
 - 13.5 Other invested assets
 - 13.6 Miscellaneous applications
 - 13.7 Total investments acquired
 - Self-explanatory – Skip
14. Net increase (decrease) in contract loans and premium notes

- Self-explanatory – Skip
15. Net cash from investments
- Self-explanatory – Skip

Cash from Financing and Miscellaneous Sources

16. Cash provided (applied):
- 16.1 Surplus notes, capital notes
 - 16.2 Capital and paid in surplus, less treasury stock
 - 16.3 Borrowed funds
 - 16.4 Net deposits on deposit-type contracts and other insurance liabilities
 - 16.5 Dividends to stockholders
 - 16.6 Other cash provided (applied)
- Self-explanatory except for line 16.6. See comments regarding lines 1 and 5. Because of GAAP accounting for reinsurance, certain items that would be more meaningful under operations are reflected in Cash flow from financing and miscellaneous sources.
17. Net cash from financing and miscellaneous sources
- Total of lines 16 through 16.6

Reconciliation of Cash, Cash Equivalents and Short-Term Investments

18. Net change in cash, cash equivalents and short-term investments
- Sum of cash flow from operations, investments and financing
19. Cash, cash equivalents and short-term investments:
- 19.1 Beginning of year
 - 19.2 End of year
- These figures are taken from the balance sheet and used to reconcile the beginning cash plus change in cash flow equal the ending cash balance

* * * * *