ICI Mutual

Annual Report 2018

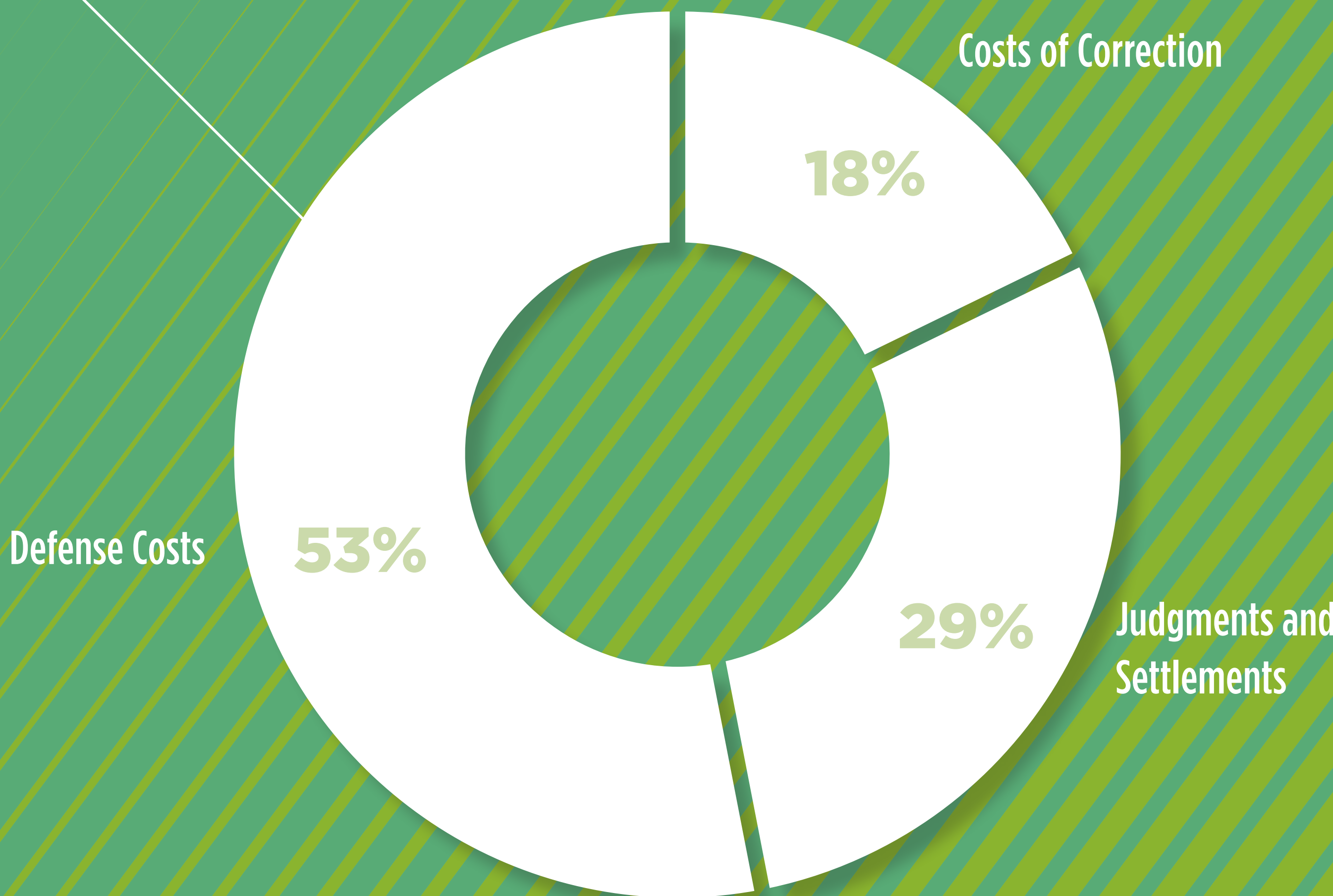
2018

STEADFAST
COMMITTED
FOCUSED

In 2018, ICI Mutual entered its fourth decade as an "industry mutual" insurer, steadfast in its commitment to its long-standing mission and to the core principles on which it was founded.

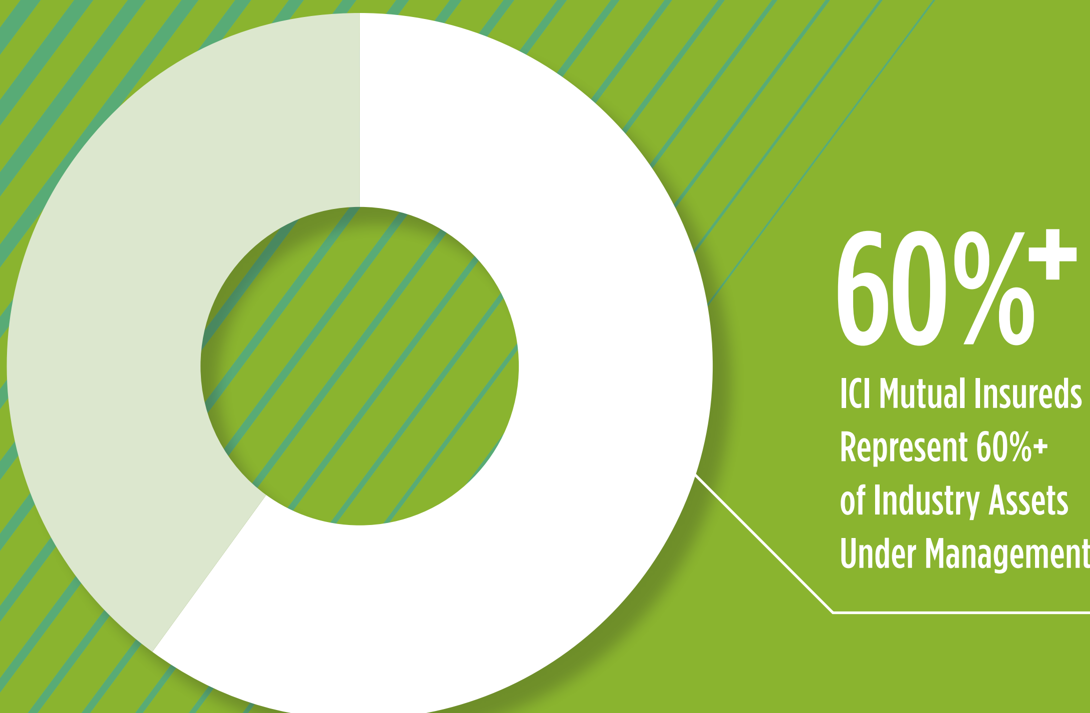
OVER $1 B

Cumulative D&O/E&O Claims Paid



ICI Mutual At A Glance

Data as of December 31, 2018



Daniel T. Steiner, President

Lawrence H. Kaplan, Chairman

A Message from the
President and the Chairman

2018 was a successful year of operations for ICI Mutual. The Company achieved its fourteenth consecutive annual underwriting profit, A.M. Best again affirmed the Company's "A" (Excellent) rating, and cumulative dividends declared by the Board of Directors over the Company's history reached $100 million.

The Company's underwriting profit, when combined with investment results, resulted in net income, after dividends and income taxes, of $8.9 million. Year-end equity nevertheless declined modestly to $272 million, due largely to the impact of market-driven unrealized losses in the Company's investment portfolio. In December, the Company's Board of Directors declared a $6 million dividend to be paid to ICI Mutual's Participating Members as a credit against their 2019 renewal premiums. Management's discussion of 2018's operating results is provided on pages 6-7.

In 2018, ICI Mutual entered its fourth decade as an "industry mutual" insurer, steadfast in its commitment to its long-standing mission and to the core principles on which it was founded. Consistent with its mission and these principles, the Company remains focused on offering insurance coverages designed and tailored to address the fund industry's specialized and evolving risks; on providing prompt, expert, and fair-minded claims handling; on making available the insurance limits requested by its member-insured fund groups at premiums rationally related to the fund industry's own risks; and on supplying its member-insured fund groups and the fund industry with a range of insurance, loss prevention, and risk management services.

The fact that the Company has delivered these benefits so consistently and for so many years is remarkable, but not surprising. For these are exactly the benefits that industry mutual insurers are designed to provide. Indeed, these benefits succinctly explain why industry mutual insurers are supported by their member-insureds and by their industries and are viewed as expert and reliable alternatives to the uncertainties and historical cyclicality of the commercial insurance markets. (Readers seeking more information on industry mutual insurers in general, and/or on the Company's role as an industry mutual insurer for the fund industry, are encouraged to review the Company's 2017 publication, *ICI Mutual Then and Now: The Enduring Value of an Industry Mutual Insurer,* available at **www.icimutual.com**.)

ICI Mutual has long played a leading role in assisting its member-insureds and the fund industry to better understand and navigate the modern claims environment.

2018 marked the 30th anniversary of the Company's commencement of active operations. (Founded in 1987, ICI Mutual began issuing policies and bonds in 1988.) Many of the Company's original member-insured fund groups (or their successors) remain insureds today. The willingness of the Company's member-insureds to take a long-term view as to the value of the Company and its mission, and their continued support of the Company over the years, have been instrumental to the Company's success and to its ability to provide the benefits outlined above.

2018 also marked the anniversary of another seminal event for the Company. Fifteen years ago, in September 2003, startling allegations of market timing and late trading in fund shares touched off what became an unprecedented firestorm of regulatory enforcement proceedings and shareholder lawsuits in the fund industry. For the industry, the fund trading scandal period ultimately resulted in lasting and beneficial regulatory and structural changes. For ICI Mutual, the period evidenced the resiliency of the Company's industry mutual model and demonstrated the Company's ability to weather a catastrophic industry event.

Looking back now, the fund trading scandal period can be seen as the opening of a "modern era" for fund industry claims. This modern era has been one in which claims—in the form of shareholder lawsuits initiated by the plaintiffs' bar, enforcement investigations and proceedings initiated by the SEC and other regulators, and operational errors requiring correction—have become, and remain, a real and ever-present risk for fund groups.

Note from the President

This coming June, Larry Kaplan will complete his term as Chairman of ICI Mutual's Board of Directors. The Company's Board and officers extend their appreciation to Larry for his leadership as Chairman and for his fourteen years of dedicated service on the Board and its committees.

Larry's knowledge, experience, and leadership have been invaluable to ICI Mutual and to its work on behalf of its member-insureds and the broader fund industry. We are pleased that he will continue to serve as a director of the Company going forward.

ICI Mutual's own experience is instructive in this regard. Of the more than $1 billion in D&O/E&O insurance claims paid (or currently reserved) by the Company since its formation, more than $850 million (76%) reflects payments (or current reserves) on claims initiated since 2003. Meanwhile, the severity of the Company's median paid (or currently reserved) claim during this 2003-2018 period (i.e., the total dollar amount of the claim, including defense costs) has more than tripled from that of 1988-2002.

ICI Mutual has long played a leading role in assisting its member-insureds and the fund industry to better understand and navigate this modern claims environment. The Company's staff members regularly present on industry claims matters to fund boards of directors and advisory personnel, and at industry-sponsored conferences and events. The Company prepares and distributes numerous publications and materials—including *Claims Trends* (an annual report on fund industry litigation and regulatory enforcement developments), *Litigation Notebook* (a database providing detailed public information on individual lawsuits and regulatory proceedings involving fund groups), and selected studies (including a 2016 study on *Section 36(b) Litigation Since Jones v. Harris*)—that offer information, analysis, and guidance on claims developments. A forthcoming ICI Mutual study, tentatively titled *Shareholder Litigation in the Fund Industry*, will examine the general nature, number, and outcomes of the hundreds of high-stakes, securities-related lawsuits that have been initiated by the plaintiffs' bar against fund groups in the 21st century. The new study is designed to serve as both a high-level introduction to "entrepreneurial litigation" risk in the modern fund industry and as a basic framework to assist advisory personnel and fund independent directors to better understand how this risk may manifest itself in the years ahead.

Most importantly, of course, the Company remains dedicated to supporting and standing behind its member-insureds when claims occur. The Company's expertise in handling specialized (and frequently complex) fund industry claims, and its cooperative and collaborative approach to the claims handling and claims resolution process, are broadly acknowledged throughout the fund industry insurance market. Both the expertise and the approach derive directly from the Company's status as an industry mutual insurer—from its mission and from the core principles on which it was founded. In these respects, as in many others, ICI Mutual continues to stand apart from its commercial insurance competitors and to provide enduring value to the fund industry it serves.

On behalf of the Company's Board of Directors and staff, we thank you, the Company's member-insureds, for your long-standing loyalty and support. As always, we invite and welcome any suggestions that you may have to ensure that ICI Mutual continues to serve your individual interests as member-insureds, along with the broader interests of the fund industry.

Daniel T. Steiner

Daniel T. Steiner
President

Lawrence H Kaplan

Lawrence H. Kaplan
Chairman of the Board of Directors

Financial Overview

Gross premiums written in 2018 were $79.3 million while net premiums earned were $28.1 million.

ICI Mutual recorded an underwriting profit of $8.2 million in 2018, the fourteenth consecutive year that underwriting income (net premiums earned) exceeded underwriting expenses (net losses incurred and G&A expenses). Income before policyholder dividends and income taxes totaled $16.9 million.

Gross premiums written in 2018 were $79.3 million while net premiums earned were $28.1 million. Gross premiums written were lower than in 2017, primarily due to decreases in "exposure" units rather than decreases in premium rates. The Company continues to promote stable, risk-related premiums, and in 2018, as in 2017, most member-insureds renewed coverages at expiring rates and coverage terms. The Company's year-over-year retention rate remained high, with over 95% of member-insureds renewing their coverage.

Net loss and loss adjustment expenses equaled $8.1 million for the year, a decrease from the $11.3 million experienced in 2017, primarily due to net favorable development on existing claims. The Company's loss ratio for 2018 (net loss and loss adjustment expenses divided by net premiums earned) was 29%. The Company's combined ratio was 71% before dividends to Participating Members, and 92% after dividends to Participating Members.

Net investment income equaled $9.5 million in 2018, higher than the 2017 amount, due to higher interest on debt securities and higher dividends on equity securities.

A policyholder dividend of $6.0 million was declared by the Company's Board of Directors in December 2018 and is payable to Participating Members that renew eligible participating policies in 2019. Income taxes, reflecting the new 21% federal income tax rate, adjusted for permanent differences, were $2.0 million. Net income, after dividends and income taxes, was $8.9 million in 2018, the same as in 2017.

Total equity decreased by approximately $1 million to $272.2 million, as a result of the $8.9 million in net income offset by a $9.9 million decrease in net unrealized appreciation on investments. In 2018, the Company maintained an "A" (Excellent) rating from A.M. Best.

Aligned Interests

Now, more than three decades on, ICI Mutual continues to be an established, trusted presence and the top provider of professional liability insurance for the mutual fund industry.

A nationwide liability insurance crisis in the mid-1980s left the mutual fund industry at risk. The industry had insurance needs that commercial insurers were unable or unwilling to meet: the need for a stable, long-term source of substantial insurance capacity; and the need for insurance pricing that could be counted upon to be reliably and rationally related to the fund industry's own risks. In 1987, fund industry leaders, working with the Investment Company Institute (the industry's trade association), formed ICI Mutual. As an industry mutual insurer, ICI Mutual is dedicated solely to serving the insurance and risk management needs of funds, fund directors and officers, and fund advisers, providing them with an expert and reliable long-term alternative to the uncertainties and cyclicality to which commercial insurance markets have historically been subject.

Now, more than three decades on, ICI Mutual continues to be an established, trusted presence and the top provider of professional liability insurance for the mutual fund industry. ICI Mutual seeks to provide insurance capacity and to ensure relative stability of premium rates and policy terms through all insurance market cycles, to craft sustainable insurance coverages tailored to address existing, new, and emerging risks faced by fund groups, to address and resolve insurance claims promptly and fairly, and to provide the fund industry with focused risk management, loss prevention, and insurance-related services and assistance. As an insurance company owned and governed by its member-insured fund groups, ICI Mutual's interests are fully aligned with the interests of its member-insureds.

The Company's Board of Directors includes fund industry executives and fund independent directors from among the Company's member-insured fund groups. Each director brings demonstrated leadership and expertise to the Board, which plays a significant role in helping to shape Company policies and initiatives. The involvement and oversight of the Board ensures that ICI Mutual is operated to serve and benefit the Company's member-insureds.

Knowledge
& Expertise

Since its formation, ICI Mutual has continuously provided fund groups with core insurance coverages that respond to the key "real world" risks long faced by funds, fund directors and officers, and fund advisers. Over the years, the Company has also developed and introduced numerous additional coverages to address the industry's new and emerging risks. ICI Mutual's professional staff has significant expertise and experience with mutual fund and investment adviser issues and consults with industry experts (including industry representatives who serve on the Company's Board of Directors) during the process of developing insurance coverages.

By reason of its detailed and comprehensive knowledge of fund industry operations and claims, ICI Mutual is uniquely positioned to analyze and understand the industry's risks, and to craft insurance coverages that are tailored to address these risks and to remain sustainable over time.

Detailed descriptions of ICI Mutual's core coverages may be found online at: www.icimutual.com/coverages. ICI Mutual also has the ability to craft custom coverages in response to particular needs of member-insureds.

Coverages

ICI Mutual's core insurance products are designed to address the specialized insurance needs of funds, fund directors and officers, and fund advisers.

The Directors and Officers/Errors and Omissions (D&O/E&O) Liability Policy protects individual directors and officers and insured companies against the financial impact of judgments, settlements, and legal defense costs incurred in shareholder lawsuits and regulatory investigations and proceedings, and the costs of correcting certain operational errors.

The Investment Company Blanket (Fidelity) Bond protects insureds against specified losses caused by employee theft, third-party fraud, and certain other types of events, and meets the basic fidelity bonding requirement for funds under the Investment Company Act of 1940.

The Independent Directors Liability (IDL) Policy provides comprehensive coverage tailored to address the concerns, and distinct insurance needs, of fund independent directors.

Services

UNDERWRITING

ICI Mutual's underwriters focus solely on the mutual fund industry and are attuned to its risks and challenges. Each member-insured fund group is assigned an underwriter who develops a thorough understanding of that fund group's business, processes, and procedures. This enables ICI Mutual to structure coverage and offer limits that appropriately reflect each member-insured's risk profile.

CLAIMS HANDLING

ICI Mutual is highly regarded for its prompt and fair-minded claims handling. Each submitted claim undergoes a careful analysis of the facts, circumstances, and applicable coverage language. ICI Mutual representatives work closely with affected member-insureds throughout the claims process.

RISK MANAGEMENT

ICI Mutual's expertise and knowledge of the fund industry are unrivaled among professional liability insurers. The Company has long provided member-insureds and the fund industry with a wide variety of risk management, loss prevention, and insurance-related services.

ICI Mutual's Risk Management Publications, listed on page 13, provide in-depth research and analysis on the fund industry's liability exposures and other topics of interest, and are designed to help member-insured fund groups improve their risk management programs and risk profiles. *Claims Trends* and the Company's online *Litigation Notebook* address existing, new, and evolving areas of regulatory and litigation exposure and their implications for insurance claims and coverage. These publications and other materials can be accessed on the Company's website (**www.icimutual.com**).

ICI Mutual sponsors an annual Risk Management Conference, at which industry experts and guest speakers present information on an array of risk management topics and facilitate discussion among risk managers, legal personnel, and other representatives of the Company's member-insureds. The Company's professional staff regularly provides individualized assistance to fund groups in structuring insurance programs, selecting among insurance options, and establishing appropriate insurance limits. The staff also responds to requests from fund boards, outside counsel, and in-house personnel for presentations, written materials, and informal advice on insurance and claims-related issues and developments.

ICI Mutual's Risk Management Publications

Insurance

Mutual Fund D&O/E&O Insurance (2009)

Independent Directors Liability (IDL) Insurance (2013)

ICI Mutual Then and Now (2017)

Claims and Litigation

Managing Defense Costs (2004)

Independent Director Litigation Risk (2006)

What to Expect in the Claims Process (2007)

Mutual Fund Prospectus Liability (2010)

ERISA Liability (2010)

Trends in Fee Litigation (2014)

Section 36(b) Litigation Since *Jones v. Harris* (2016)

Industry Risks and Risk Management

Managing Risk in Processing Corporate Actions (2001)

Investment Management Compliance Risks (2002)

Understanding Bond Fund Risks (2002)

Fair Valuation Study—An Introduction (with ICI and IDC) (2005)

Fair Valuation Study—The Role of the Board (with ICI and IDC) (2006)

Preparing for a Pandemic (2007)

Managing Risks in Trade Allocation (2008)

Outsourcing by Advisers and Affiliated Service Providers (2008)

Managing Operational Risks of Private Accounts (2011)

Technology-Related Risks

Computer Security Lite (2003)

The Two Faces of Identity Theft (2006)

Risk Management in the Digital Age (2012)

Shareholder Authentication (2015)

Financial Stability

For over three decades, ICI Mutual has stood behind its member-insureds through significant financial market and fund industry-wide events, and has prospered through various economic and insurance cycles.

ICI Mutual's financial success can be attributed to its philosophy of conservative management in every aspect of its business. From underwriting to portfolio management to administration, the Company strives to use resources wisely, to invest prudently, and to manage risk effectively. Through adherence to this philosophy, ICI Mutual has developed and maintained the financial strength and stability necessary to meet the needs of its member-insureds.

For over three decades, ICI Mutual has stood behind its member-insureds through significant financial market and fund industry-wide events, and has prospered through various economic and insurance cycles. The Company utilizes its strong network of reinsurance partners to manage and diversify its own risk, enabling it to provide the full limits of coverage required by member-insureds and to promote relative stability of premium rates and coverage terms.

As an integral part of the fund industry, ICI Mutual provides a consistent and readily available source of insurance capacity, at premiums rationally related to the fund industry's own risks.

Board
of Directors

Lawrence H. Kaplan, Chairman (E, N)
Lord, Abbett & Co. LLC

Barry Fink, Vice Chairman (E, I, N)
American Century Funds

James H. Bodurtha**
BlackRock Mutual Funds

Martin A. Burns (R)
Investment Company Institute

Kevin M. Carome (U)
Invesco Ltd.

Joseph A. Carrier (R, N)
Legg Mason, Inc.

Stefanie Chang Yu (E, U)
Morgan Stanley

Kenneth C. Eich (E, A)
Davis Selected Advisers, L.P.

Ronald H. Fielding (I)
Saturna Investment Trust

Keith R. Fox CFA (I)
DWS Funds

Maureen A. Gemma (R)
Eaton Vance Management

Robert F. Gunia (I)
Prudential Insurance Mutual Funds

Heidi W. Hardin (U, N)
MFS Investment Management

William V. Healey (E, U)
Allianz Global Investors U.S. Holdings LLC

Diana P. Herrmann (A, R)
Aquila Investment Management LLC

Steven M. Joenk (U)
AXA Equitable Life Insurance Company

Michael L. Kimmel (R)
Vanguard

Les M. Kratter (A)
Franklin Resources, Inc.

Paul S. Kulig (A)
Facey Goss and McPhee P.C.

James J. McMonagle*
Selected Funds

David Oestreicher (E, I, R)
T. Rowe Price Associates, Inc.

David M. Pfeffer (A)
OppenheimerFunds, Inc.

Carmelo Spinella (U)
Capital Research and Management Company

Daniel T. Steiner (E, I, R)
ICI Mutual Insurance Company, RRG

Paul Schott Stevens (E, U)
Investment Company Institute

George C. W. Gatch, Ex-Officio
J.P. Morgan Asset Management

Board Committees:

Executive (E), Audit (A), Investment (I), Underwriting (U), Risk Management (R), Nominating (N)

* On Sabbatical

** Retired from ICI Mutual Board of Directors Effective December 31, 2018

Pictured left to right:

David Oestreicher
Paul S. Kulig
Heidi W. Hardin
Steven M. Joenk
Les M. Kratter
Carmelo Spinella

Keith R. Fox
Daniel T. Steiner
Stefanie Chang Yu
Robert F. Gunia
James H. Bodurtha
Kenneth C. Eich

Lawrence H. Kaplan
Ronald H. Fielding
Barry Fink
William V. Healey
Diana P. Herrmann
Joseph A. Carrier

Not pictured: Martin A. Burns, Kevin M. Carome, Maureen A. Gemma, Michael L. Kimmel, James J. McMonagle, David M. Pfeffer, Paul Schott Stevens

Officers and Staff

Officers

Daniel T. Steiner
President

John T. Mulligan
Senior Vice President and Chief Underwriting Officer

Julia S. Ulstrup
Vice President, General Counsel and Assistant Secretary

Charles G. Preseau
Vice President and Chief Financial Officer

Paul S. Kulig
Secretary-Treasurer

Staff

William Y. Akishev
Director, Information Technology

Virginia S. Barry
Associate Counsel

Meloney G. Burrell
Senior Accountant

Catherine M. Dalton
Underwriting Manager

Briana R. Davis
Lead Broker

John D. Driggers
Director, Data Analytics

Prabhat S. Friedland
Underwriting Analyst

Michael A. Heiser
Controller

Lizabeth S. Hurst
Corporate Communications

Carolyn B. Julia
Executive Assistant

Swenitha Nalli
Underwriter

Samy S. Rabb
Underwriter

Shafat Rahman
Senior Accountant

Colin K. Rouse
Assistant Controller

Margaret M. Sullivan
Director, Underwriting Department

David U. Thomas
Senior Associate Counsel and Director, Cyber Risk Issues

Amy P. Veloz
Legal Insurance Assistant

Jinhua Zhang*
Director, Corporate Reporting

**Retired December 31, 2018*

Selected **Financial Highlights**

For the Years Ended	2018	2017
Gross Premiums Written	$ 79,264	$ 80,355
Net Premiums Earned	$ 28,116	$ 29,572
Net Loss and Loss Adjustment Expenses	$ 8,070	$ 11,323
Net Underwriting Profit	$ 8,159	$ 6,581
Net Investment Income	$ 9,502	$ 9,326
Dividends to Policyholders	$ 5,999	$ 5,954
Net Income	$ 8,927	$ 8,859
Total Equity	$ 272,165	$ 273,142
Combined Ratio		
Loss and General Expense Ratio	71%	78%
Policyholder Dividends	21%	20%
Combined Ratio including Policyholder Dividends	92%	98%

ICI Mutual Insurance Company,
A Risk Retention Group

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2018

Consolidated Financial Statements

ICI MUTUAL Insurance Company
A Risk Retention Group

Report of Independent Auditors

To the Board of Directors of
ICI Mutual Insurance Company, a Risk Retention Group:

We have audited the accompanying consolidated financial statements of ICI Mutual Insurance Company, a Risk Retention Group, and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations, changes in equity and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of ICI Mutual Insurance Company, a Risk Retention Group, and its subsidiaries as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP, 101 Seaport Boulevard, Boston, MA 02210
T: (617) 530 5000, F: (617) 530 5001, www.pwc.com/us

Other Matter

Accounting principles generally accepted in the United States of America require that the incurred and paid claims development disclosure on pages 28 to 29 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers LLP

Boston, Massachusetts
April 18, 2019

ICI Mutual Insurance Company, a Risk Retention Group
Consolidated Balance Sheets
December 31, 2018 and 2017 (in 000's)

	2018	2017
Assets		
Cash and cash equivalents	$ 11,730	$ 14,311
Investments		
Debt securities, at fair value (amortized cost of $268,455 and $268,434, respectively)	264,877	271,968
Equity securities, at fair value (cost of $28,692 and $28,677, respectively)	55,003	60,362
Money market funds	86	637
Total cash and investments	331,696	347,278
Prepaid expenses	524	465
Prepaid federal and state income taxes	1,607	2,443
Deferred policy acquisition costs	2,450	2,517
Premiums receivable	12,554	6,963
Interest receivable	1,899	1,929
Reinsurance recoverables	93,181	94,090
Prepaid reinsurance premiums	34,231	34,282
Other amounts receivable under reinsurance contracts	2,967	3,664
Furniture and fixtures, net	968	1,129
Deferred income taxes	647	-
Total assets	$ 482,724	$ 494,760
Liabilities and Equity		
Reserve for losses and loss adjustment expenses	$ 137,932	$ 147,299
Unearned premiums	46,215	46,712
Reinsurance premiums payable	5,608	5,839
Premium taxes payable	613	542
Deferred income taxes	-	2,173
Accounts payable and other liabilities	3,723	3,364
Benefits payable	10,406	9,427
Dividends payable	6,062	6,262
Total liabilities	210,559	221,618
Contingencies (Note 10)		
Contributed surplus	18,198	18,200
Accumulated other comprehensive income	14,831	20,562
Accumulated earnings	239,136	234,380
Total equity	272,165	273,142
Total liabilities and equity	$ 482,724	$ 494,760

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

ICI Mutual Insurance Company, a Risk Retention Group
Consolidated Statements of Operations
Years Ended December 31, 2018 and 2017 (in 000's)

	2018	2017
Revenues		
Net premiums written	$ 27,669	$ 28,622
Change in net unearned premiums	447	950
Net premiums earned	28,116	29,572
Net investment income	9,502	9,326
Net realized (losses) gains on securities	(1,093)	139
Other income	323	324
Total revenues	36,848	39,361
Expenses		
Net loss and loss adjustment expenses	8,070	11,323
Underwriting, general and administrative expenses	11,887	11,668
Total expenses	19,957	22,991
Income before dividends to policyholders and provision for income taxes	16,891	16,370
Dividends to policyholders	5,999	5,954
Income before provision for income taxes	10,892	10,416
Provision for income taxes	1,965	1,557
Net income	8,927	8,859
Other Comprehensive Income		
Net unrealized (losses) gains on securities:		
Net unrealized (losses) gains arising during the period, net of tax	(10,727)	8,960
Reclassification adjustment for losses (gains) realized in net income, net of tax	863	(92)
Net actuarial unrealized (losses) gains on employee benefit plans:		
Net unrealized (losses) gains arising during the period, net of tax	(269)	115
Reclassification adjustment for losses realized in net income, net of tax	231	293
Other comprehensive (loss) income, net of tax, net of reclassification adjustments	(9,902)	9,276
Comprehensive (loss) income	$ (975)	$ 18,135
Net realized (losses) gains on securities		
Other net realized investment (losses) gains	$ (1,093)	$ 139
Net realized (losses) gains on securities	$ (1,093)	$ 139

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

ICI Mutual Insurance Company, a Risk Retention Group
Consolidated Statements of Changes in Equity
Years Ended December 31, 2018 and 2017 (in 000's)

	Contributed Surplus	Accumulated Other Comprehensive Income	Accumulated Earnings	Total Equity
Balance at December 31, 2016	$ 18,200	$ 11,286	$ 225,521	$ 255,007
Net income	-	-	8,859	8,859
Other comprehensive income, net of tax, net of reclassification adjustments	-	9,276	-	9,276
Distributions of contributed surplus	-	-	-	-
Balance at December 31, 2017	$ 18,200	$ 20,562	$ 234,380	$ 273,142
Net income	-	-	8,927	8,927
Other comprehensive loss, net of tax, net of reclassification adjustments	-	(9,902)	-	(9,902)
Reclassification of deferred tax effects	-	4,171	(4,171)	-
Distributions of contributed surplus	(2)	-	-	(2)
Balance at December 31, 2018	$ 18,198	$ 14,831	$ 239,136	$ 272,165

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

ICI Mutual Insurance Company, a Risk Retention Group
Consolidated Statements of Cash Flows
Years Ended December 31, 2018 and 2017 (in 000's)

	2018	2017
Cash Flows from Operating Activities		
Net income	$ 8,927	$ 8,859
Adjustments to reconcile net income to net cash used in operating activities		
Amortization of premium	826	1,118
Deferred income taxes	(189)	(1,206)
Depreciation and amortization	166	195
Net realized (losses) gains on securities	1,093	(139)
Changes in operating assets and liabilities		
Prepaid expenses	(59)	54
Prepaid federal and state income taxes	836	(1,042)
Deferred policy acquisition costs	67	122
Premiums receivable	(5,591)	632
Interest receivable	30	64
Reinsurance recoverables	909	94,288
Prepaid reinsurance premiums	51	2,321
Other amounts receivable under reinsurance contracts	697	(1,026)
Reserve for losses and loss adjustment expenses	(9,367)	(105,635)
Unearned premiums	(497)	(3,272)
Reinsurance premiums payable	(231)	(723)
Premium taxes payable	71	(126)
Accounts payable and other liabilities	359	7
Benefits payable	932	545
Dividends payable	(200)	211
Net cash used in operating activities	(1,170)	(4,753)
Cash Flows from Investing Activities		
Proceeds from sales of investments available for sale	82,464	71,517
Proceeds from maturities of investments available for sale	7,965	4,445
Purchases of furniture and fixtures	(5)	(143)
Payments for purchases of investments available for sale	(92,384)	(71,162)
Change in money market funds	551	938
Net cash (used in) provided by investing activities	(1,409)	5,595
Cash Flows from Financing Activities		
Distributions of contributed surplus	(2)	-
Borrowing from the FHLB	20,000	15,000
Repayment to the FHLB	(20,000)	(15,000)
Net cash used in financing activities	(2)	-
Net (decrease) increase in cash and cash equivalents	(2,581)	842
Cash and cash equivalents at beginning of year	14,311	13,469
Cash and cash equivalents at end of year	$ 11,730	$ 14,311

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

1. Significant Accounting Policies

A. Basis of Presentation

ICI Mutual Insurance Company ("Mutual") was incorporated on August 26, 1987 as an association captive insurance company domiciled in the State of Vermont and commenced accepting insurance risks on March 1, 1988. Mutual, together with its wholly owned subsidiaries described below, are collectively referred to as "the Company." The Company primarily writes fidelity bonds and directors and officers and errors and omissions insurance for Members and Associate Members of the Investment Company Institute ("ICI") and their affiliated companies on a claims-made basis. These Members primarily provide services to the regulated investment company industry. On January 1, 2009, the Company converted from a Vermont association captive insurance company to a Vermont risk retention group ("RRG"), under the Federal Liability Risk Retention Act.

ICI Mutual Insurance Brokers, Inc. ("Brokers") is a wholly-owned subsidiary of Mutual. Brokers provides insurance brokerage services to insureds of Mutual.

ICIM Services, Inc. ("Services") is a wholly-owned subsidiary of Mutual. Services provides the underwriting function for Mutual under a written agreement. This agreement provides that Mutual will reimburse Services for all reasonable expenses associated with performing the underwriting function plus a 5% fee.

The Consolidated Financial Statements include the consolidated accounts of Mutual, Brokers, and Services, with all significant intercompany amounts eliminated in consolidation. The Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"), which are also in accordance with practices prescribed for RRGs by the Vermont Department of Financial Regulation ("VDFR").

GAAP requires management to make certain estimates and assumptions in the preparation of the financial statements. Actual results could differ from those estimates and assumptions.

B. Investments

The Company's debt and equity securities are classified as available-for-sale and reported at fair value as defined in Note 3. Short-term securities and money market funds are stated at amortized cost which approximates fair value.

For securities where the fair value is less than the amortized cost basis for debt securities and cost for equity securities, the Company must determine whether or not an other-than-temporary impairment has occurred. See Note 2 for a detailed explanation of the procedures utilized by the Company in calculating other-than-temporary impairment losses.

All debt investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying trading and investing positions. To manage credit risk, the Company focuses on higher quality fixed income securities, limits its exposure in any one investment, and monitors the portfolio quality, taking into account credit ratings assigned by recognized statistical rating organizations.

Interest income on debt securities is recorded on the accrual basis. Dividend income on equity securities is recorded on the ex-dividend date. Unrealized gains and losses from changes in the fair value of the Company's holdings, net of applicable federal income taxes, are reported as a separate component of equity. Realized gains and losses on the sale of the Company's securities are determined based on specific identification and are included as a separate component of operations.

C. Premiums

Net earned premiums have been computed on a semimonthly pro rata basis over the term of the underlying insurance policies with the exception of premiums on "tail" policies which are earned when written. Ceded reinsurance premiums are charged against premiums earned on the same basis. Unearned premiums represent the portion of the gross premium written which is applicable to the unexpired terms of policies in force. Prepaid reinsurance premiums represent the portion of unearned premiums ceded to reinsurers. Commissions on reinsurance premiums ceded are earned when due and are reflected as a reduction to ceded reinsurance premiums.

D. Deferred Policy Acquisition Costs

Acquisition costs consist primarily of underwriter compensation, fees and premium taxes associated with the successful acquisition and underwriting of new and renewal insurance business. These acquisition costs are being amortized over the expected policy period of related policies in proportion to the ratio of the annual earned premiums to the total premium revenue anticipated. Anticipated premium revenue was estimated using the same assumptions as those used for computing the reserve for losses and loss adjustment expenses. Expected losses, related expenses, and investment income are considered in measuring the recoverability of this asset.

E. Reserve for Losses and Loss Adjustment Expenses

The reserve for losses and loss adjustment expenses is based on management's individual case estimates of the ultimate cost of reported losses and estimates for incurred but not reported losses ("IBNR") determined in consultation with independent professional actuaries. The method of making IBNR estimates and for establishing the resulting reserves is based on actuarial assumptions as to future contingencies and as to the applicability of other data sources which the Company's independent actuaries deem to be reasonable and appropriate in the circumstances. However, given the nature of the Company's business, the ultimate amount of losses and loss adjustment expenses may vary significantly from the estimated amounts. Due to this uncertainty, the appropriateness of the current level of such estimated liability can only be determined with the passage of time. Any adjustments to these estimates, which could be significant, will be reflected in income in the period in which the estimates are changed or payments are made.

F. Provision for Income Taxes

The Company accounts for income taxes in accordance with Accounting Standards Codification (ASC) 740, "Accounting for Income Taxes." The codification requires that deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Valuation allowances are established when necessary to reduce deferred tax assets to an amount that, in the opinion of management, is more likely than not to be realized. No valuation allowance was deemed necessary at December 31, 2018 and 2017.

The guidance on accounting for uncertainty in income taxes describes how uncertain tax positions should be recognized, measured, presented and disclosed in the financial statements. This guidance requires the evaluation of tax positions taken or expected to be taken in the course of preparing the Company's financial statements to determine whether the tax positions are "more-likely-than-not" to be sustained by the applicable tax authority. Tax positions not deemed to meet the "more-likely-than-not" threshold would be recorded as a tax benefit or expense in the current year. If applicable, interest and penalties are classified as other interest expense and are included in underwriting, general and administrative expenses in the Consolidated Statements of Operations. There were no interest or penalties incurred in 2018 or 2017.

On December 22, 2017, the "Tax Cuts and Jobs Act" ("TCJA" or "Tax Act") was signed into law. The provisions of TCJA include a broad range of tax reform provisions that are applicable to the Company, including a reduction in the U.S. corporate income tax rate that the Company is generally subject to from 35% to 21% effective January 1, 2018. In accordance with the provisions of ASC 740 , changes in tax rates and tax law are accounted for in the period of enactment, which is the date the President signed the bill into law and are recorded as a component of the income tax provision related to continuing operations.

Given the short timing between the enactment date and calendar year-end reporting deadlines, on December 22, 2017, the SEC staff issued Staff Accounting Bulletin No. 118 ("SAB 118"), with similar provisions extended by the FASB staff for non-public companies, to address the application of U.S. GAAP in situations when a registrant did not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting in its annual 2017 financial statements for certain income tax effects of the 2017 Tax Act. Pursuant to the guidance, a Company fell into one of three scenarios: accounting was (1) complete for the tax effects of the 2017 Tax Act, (2) incomplete but a reasonable estimate can be determined, or (3) incomplete. To the extent the accounting was incomplete, the guidance provided for a measurement period not to extend beyond one year of the enactment date.

Additionally, pursuant to INT 18-01: Updated Tax Estimates Under the Tax Cuts and Jobs Act, the NAIC adopted similar concepts related to "complete" and "incomplete" estimates and those for which a reasonable estimate could be determined. It also provided a limited time exception to NAIC

Statement on Statutory Accounting Principles ("SSAP") 9, Subsequent Events (one year from enactment date), which allowed companies not to adjust the audited financial statements when there was a change in estimate of year-end 2017 amounts after the Annual Statement had been filed.

As of December 31, 2017, the Company had not completed its accounting for the effects of the TCJA on certain deferred tax balances; however, it made provisional estimates of those amounts in accordance with the guidance above. Accordingly, the Company recorded a provisional benefit of approximately $1.5 million for the year ended December 31, 2017. As of December 31, 2018, the Company completed the collection, preparation, and analysis of data relevant to the TCJA, and interpreted any additional guidance issued by the IRS, U.S. Department of the Treasury, or other standard-setting organizations, and did not recognize any material changes in its provision for income taxes. Refer to Note 6 for the nature and amount of the measurement period adjustment and the impact on the effective tax rate.

G. Reinsurance

The Company utilizes both treaty and facultative reinsurance to provide protection for claims in excess of the Company's normal retention limits ($3 million). Under the Company's annual treaty reinsurance program (which runs from April 1 to March 31), limits up to $15 million, less the Company's normal retention, are automatically assumed by the treaty participants. For the treaty years ending March 31, 2012 through 2016, the Company retains an additional $2.5 million in excess of the first $15 million recoverable.

Maximum recoveries under the reinsurance treaties are capped at $100 million for all treaty years subsequent to the treaty year ending March 31, 2005. A treaty year remains open until all noticed claims are paid or otherwise closed. As of December 31, 2018, ceded losses under all of the open treaty years were well below the respective treaty caps. Future adverse development on any of the treaty years could result in the respective caps for such treaty years being exceeded and such excess amounts, if any, would have to be paid out of the Company's earnings and surplus. While management believes that the Company is adequately capitalized to meet its ongoing claims obligations, there can be no assurance that in the event a cap on a reinsurance treaty is exceeded, the Company's resources would be sufficient to meet all of its claims liabilities.

For those insureds that require limits in excess of $15 million on Fidelity Bonds, the Company issues additional limits of up to $5 million. For limits above $20 million on Fidelity Bonds or $15 million on D&O/E&O Policies, the Company purchases facultative (case by case) reinsurance from various other reinsurers. There is no cap on facultative reinsurance except for the actual limits reinsured. In addition, the Company can elect to retain additional limits in the excess layers, generally not more than $5 million per policy.

Although reinsurance agreements contractually obligate the Company's reinsurers to reimburse it for their proportionate shares of losses, they do not discharge the primary responsibility of the Company. Thus, in the event a reinsurer did not meet its obligation under its agreement with the Company, the Company would be responsible for such amount.

The Company monitors the credit worthiness of its reinsurers and only conducts business with reinsurers that are highly rated by reputable rating agencies. As of December 31, 2018, the Company had no reason to believe that any amounts currently due from reinsurers will prove uncollectible. Accordingly, the Company has not made a separate provision for any amounts that might ultimately prove to be uncollectible from reinsurers in the future.

H. Cash and Liquidity

The Company considers all cash on hand and deposits in banks as cash and cash equivalents for purposes of the Consolidated Statements of Cash Flows. As of December 31, 2018 and 2017, the Company held $0 in cash equivalents.

The Company maintains liquid investments in amounts considered sufficient to pay claims and other operating expenses. It is also part of the Company's strategy to utilize its membership in the FHLB as a backup liquidity facility. The maximum amount the Company borrows fluctuates based on the amount of eligible collateral the Company holds at any given time, as well as on the amount of its investment in FHLB capital stock. As part of its liquidity strategy, the Company borrowed and repaid short-term loans of $20 million and $15 million from the FHLB in 2018 and 2017, respectively.

I. Furniture and Fixtures

Furniture and fixtures are stated at cost net of accumulated depreciation. The costs of significant additions and improvements, including leasehold improvements, are capitalized while expenditures for maintenance, repairs, and minor renewals are charged to expense as incurred. When assets are retired or otherwise disposed of, the assets and related accumulated depreciation and amortization are eliminated from the accounts and any resulting gain or loss is reflected in income. Depreciation of leasehold improvements is offset by the amortization of a rent incentive allowance. Provisions for depreciation are computed using the straight-line method based on useful lives ranging from three to twelve years. Depreciation expense was $166 and $195 for 2018 and 2017, respectively. Accumulated depreciation totaled $714 and $818 at December 31, 2018 and 2017, respectively.

J. Recent Accounting Pronouncements

Recently Adopted Accounting Standards

In February 2018, the FASB issued accounting standard update ("ASU") 2018-02 intended to help clarify certain "stranded" income tax effects in accumulated other comprehensive income (AOCI) resulting from tax reform. The ASU allows companies to reclassify stranded income tax effects from AOCI to retained earnings. These amendments are effective for fiscal years beginning after December 31, 2018, however early adoption is permitted. The Company early adopted this guidance effective January 1, 2018, and as a result, reclassified all stranded income tax effects resulting from tax reform on an aggregate portfolio basis, by increasing AOCI and decreasing Accumulated Earnings, each by $4.2 million, as reported in the Consolidated Statements of Changes in Equity. There was no total impact on Equity as a result of this reclassification.

Recently Issued Accounting Standards Not Yet Adopted

In January 2016, the FASB issued ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10), Recognition and Measurement of Financial Assets and Financial Liabilities. The amendments in this ASC update address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01: (1) requires equity investments (except those accounted for under the equity method or those that result in the consolidation of the investee) to be measured at fair value with changes in the fair value recognized in net income; (2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (3) requires the use of the exit price notion when measuring the fair value of financial instruments for disclosure purposes; and (4) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the notes to the financial statements. These amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. As required upon adoption, the unrealized gains on equity securities in AOCI of $20,786, net of tax, as of December 31, 2018, will be reclassified from AOCI to Accumulated Earnings as of January 1, 2019. There will be no total impact on Equity as a result of this reclassification.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). ASU 2016-02 requires the recognition of lease assets and lease liablities by lessees for those leases classified as operating leases under previous GAAP. Under existing guidance, recognition of lease assets and liabilities is not required for operating leases. The lease assets and liabilities to be recognized are both measured initially based on the present value of the lease payments. For non-public entities, the amendments for ASU 2016-02 are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. The Company is evaluating the impact of ASU 2016-02 on its financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 replaces the existing incurred losses methodology for estimating allowances with a current expected credit losses methodology with respect to most financial assets measured at amortized cost and certain other instruments, including trade and other receivables, loans, held to maturity investment securities and off-balance sheet commitments. In addition, ASU 2016-13 requires credit losses relating to available for sale ("AFS") debt securities to be recorded through an allowance for credit losses rather than a reduction of the carrying amount. For non-public entities, the amendments in ASU 2016-13 are effective for annual and interim periods beginning after December 15, 2020. The Company is evaluating the impact of ASU 2016-13 on its financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. ASU 2016-15 reduces diversity in practice in how certain transactions are classified in the statement of cash flows. The amendments in ASU 2016-15 provide guidance on specific cash flow issues including debt prepayment or debt extinguishment costs, settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, and distributions received from equity method investees. ASU 2016-15 is effective for annual and interim periods beginning after December 15, 2018. The Company does not expect the adoption of ASU 2016-15 to have a material impact to its Consolidated Statements of Cash Flows.

In March 2017, FASB issued ASU 2017-07, Compensation Retirement Benefits. ASU 2017-07 requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. ASU 2017-07 is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. The Company is evaluating the impact of ASU 2017-07 on its financial statements.

K. Reclassifications

Certain amounts in prior year's Consolidated Financial Statements and Notes thereto have been reclassified to conform to the 2018 presentation.

L. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before the financial statements are issued or are available to be issued. The Company has evaluated all such events occurring subsequent to the balance sheet date herein of December 31, 2018 and through the date the financial statements were available to be issued, April 18, 2019. The effects of all subsequent events that provided additional evidence about conditions that existed at the date of the balance sheet, including estimates, if any, have been recognized in the accompanying Consolidated Balance Sheet and Consolidated Statement of Operations as of and for the year ended December 31, 2018. The Company did not recognize any subsequent events that provided evidence about conditions that arose after the balance sheet date.

Notes to Consolidated Financial Statements (in 000's)

2. Investments

A summary comparison of amortized cost and fair value of debt securities is as follows:

	December 31, 2018			
Debt securities available for sale	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government, agencies and authorities securities	$ 37,157	$ 656	$ (492)	$ 37,321
Mortgage-backed	85,783	349	(1,568)	84,564
All other corporate bonds	145,515	1,041	(3,564)	142,992
Total debt securities	$ 268,455	$ 2,046	$ (5,624)	$ 264,877

	December 31, 2017			
Debt securities available for sale	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government, agencies and authorities securities	$ 47,524	$ 1,059	$ (508)	$ 48,075
Mortgage-backed	62,644	445	(437)	62,652
All other corporate bonds	158,266	3,929	(954)	161,241
Total debt securities	$ 268,434	$ 5,433	$ (1,899)	$ 271,968

The amortized cost and fair value of debt securities at December 31, 2018, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due in one year or less	$ 12,252	$ 12,250
Due after one year through five years	38,775	38,555
Due after five years through ten years	74,933	73,439
Due after ten years	142,495	140,633
Total debt securities	$ 268,455	$ 264,877

Notes to Consolidated Financial Statements (in 000's)

A summary comparison of cost and fair value of equity securities is as follows:

	December 31, 2018			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Common stock	$ 28,692	$ 26,311	$ -	$ 55,003

	December 31, 2017			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Common stock	$ 28,677	$ 31,685	$ -	$ 60,362

Included in equity securities in the Consolidated Balance Sheet as of December 31, 2018 and 2017 is $185 and $170 in restricted FHLB stock, respectively.

At December 31, 2018 and 2017, the gross unrealized gains on investments in debt and equity securities of $22,733 and $35,219, respectively, have been reflected in the Consolidated Balance Sheets as a component of accumulated other comprehensive income, net of deferred taxes of $4,774 and $12,161, respectively.

There are three key investment risks that can impact the Company's investment portfolio: Liquidity Risk, Credit Risk and Market Risk.

1. **Liquidity Risk**: Market conditions create a situation where liquid assets become illiquid. To offset this risk, the Company maintains significant holdings in U.S. Treasury securities and other relatively liquid securities, a relatively short investment portfolio duration, and membership in the FHLB.

2. **Credit Risk**: An issuer (or counterparty) is unable to pay their claim and defaults. To offset this risk, the Company maintains a well-diversified portfolio containing high quality fixed income securities; 98% of these securities are rated investment grade (BBB- or higher). The portfolio is also closely monitored for downgrades on corporate bonds and cash flows on structured securities.

3. **Market Risk:** Falling market value due to changing risks in a sector or interest rate risks. The Company monitors actual concentrations against both its investment guidelines and market conditions.

Notes to Consolidated Financial Statements (in 000's)

Unrealized loss position securities:

Debt securities available for sale	Fair Value	Gross Unrealized Losses < 12 months	Gross Unrealized Losses > 12 months	Total Gross Unrealized Losses	Numbers of Investment Positions
	December 31, 2018				
U.S. Government, agencies and authorities securities	$ 16,978	$ (240)	$ (252)	$ (492)	8
Mortgage-backed	64,375	(451)	(1,117)	(1,568)	72
All other corporate bonds	94,422	(2,052)	(1,512)	(3,564)	122
Total debt securities	$ 175,775	$ (2,743)	$ (2,881)	$ (5,624)	202
Equity securities					
Stock mutual fund	-	-	-	-	-
Total equity securities	$ -	$ -	$ -	$ -	-

Debt securities available for sale	Fair Value	Gross Unrealized Losses < 12 months	Gross Unrealized Losses > 12 months	Total Gross Unrealized Losses	Numbers of Investment Positions
	December 31, 2017				
U.S. Government, agencies and authorities securities	$ 25,177	$ (251)	$ (257)	$ (508)	21
Mortgage-backed	35,694	(191)	(246)	(437)	49
All other corporate bonds	47,633	(160)	(794)	(954)	67
Total debt securities	$ 108,504	$ (602)	$ (1,297)	$ (1,899)	137
Equity securities					
Stock mutual fund	-	-	-	-	-
Total equity securities	$ -	$ -	$ -	$ -	-

The Company does not have the intent to sell, nor is it more likely than not that the Company will be required to sell, securities in unrealized loss positions that are not other-than-temporarily impaired, before recovery.

Other-Than-Temporary Impairment Evaluations

The Company reviews its investment securities regularly and determines whether other-than-temporary impairments have occurred. For fixed maturities, if a decline in fair value is judged by management to be other-than-temporary, and the Company does not intend to sell the security and it is not more likely than not that it will be required to sell the security prior to recovery of the security's amortized cost, the impairment is bifurcated into (a) the amount of the total impairment related to the credit loss, and (b) the amount of the total impairment related to interest and all other factors. The amount of the other-than-temporary impairment related to the credit loss is recognized by a charge to total other-than-temporary impairment losses in the Consolidated Statements of Operations, establishing a new cost basis for the security. The amount of the other-than-temporary impairment related to all other factors is recognized in other comprehensive income in the Statements of Operations. The factors considered by management in its regular review include, but are not limited to: the length of time and extent to which the fair value has been less than amortized cost; the financial condition and near-term prospects of the issuer; adverse changes in ratings announced by one or more rating agencies; subordinated credit support; whether the issuer of a debt security has remained current on principal and interest payments; current expected cash flows; whether the decline in fair value appears to be issuer specific or, alternatively, a reflection of general market or industry conditions (including, in the case of fixed maturities, the effect of changes in market interest rates); and the Company's intent to sell, or requirement to sell, the debt security before the anticipated recovery of its remaining amortized cost basis.

In assessing corporate debt securities for other-than-temporary impairment, the Company evaluates the ability of the issuer to meet its debt obligations and the value of the company or specific collateral securing the debt position. When evaluating whether a mortgage-backed security is other-than-temporarily impaired, the Company examines characteristics of the underlying collateral, such as delinquency and default rates, the quality of the underlying borrower, the type of collateral in the pool, the vintage year of the collateral, subordination levels within the structure of the collateral pool, the Company's intent to sell the security and whether it more likely than not will be required to sell the security before the recovery of its amortized cost basis. For all debt securities evaluated for other-than-temporary impairment (for which the Company does not have the intent to sell and it is not more likely than not that it will be required to sell the security before the recovery of its amortized cost basis), the Company considers the timing and amount of the cash flows.

The Company evaluates its mortgage-backed securities for other-than-temporary impairment using multiple inputs. Loan level defaults are estimated using appropriate modeling techniques. All bonds are modeled individually and each bond is assigned a custom default assumption based on projections for the mortgage pool, historical underlying collateral performance, and borrower characteristics.

Basic inputs to the model include data on:

- voluntary prepayments,
- defaults and,
- expected severity of losses in a liquidation scenario, taking into account loan size, geographic concentration, and loan to value percentages.

Additional variables are applied to each mortgage pool specific to structural elements such as triggers and financial guarantees to the extent that they exist. The cash flows generated by the collateral securing these securities are then determined with these default, loss severity and prepayment assumptions. These collateral cash flows are then utilized, along with consideration for the issuer's position in the overall structure, to determine the cash flows associated with the mortgage-backed security held by the Company.

Notes to Consolidated Financial Statements (in 000's)

To the extent that the present value of the cash flows generated by a debt security is less than the amortized cost, a credit loss exists, and an other-than-temporary impairment is recognized through earnings. It is reasonably possible that further declines in estimated fair values of such investments, or changes in assumptions or estimates of anticipated recoveries and/or cash flows, may cause further other-than-temporary impairments in the near term, which could be significant.

In addition, the Company evaluates other asset-backed securities for other-than-temporary impairment (OTTI) by examining similar characteristics referenced above for mortgage-backed securities. The Company evaluates U.S. Treasury securities and obligations of U.S. Government corporations, U.S. Government agencies, and obligations of states and political subdivisions for other-than-temporary impairment by examining similar characteristics referenced above for corporate debt securities.

The Company also evaluates equity securities for OTTI when fair value is less than cost. Equity securities may experience other-than-temporary impairment based on the prospects for full recovery in value in a reasonable period of time and the Company's ability and intent to hold the security to recovery. If a decline in fair value is judged by management to be other-than-temporary, a loss is recognized by a charge to total other-than-temporary impairment losses in the consolidated statements of operations. For the purpose of other-than-temporary impairment evaluations, preferred stocks are treated in a manner similar to debt securities.

Other-than-temporary impairments included in net realized losses on securities in the Consolidated Statements of Operations were $0 in both 2018 and 2017.

Further deterioration in credit quality of the companies backing the securities, deterioration in the condition of the financial services industry, imbalance in liquidity in the marketplace, a worsening of the current economic environment, or additional declines in real estate values could affect the fair value of these securities and increase the potential that certain unrealized losses be designated as other-than-temporary in future periods and the Company may incur additional write-downs.

Proceeds from sales of debt securities and the associated gross realized gains and gross realized losses are as follows:

	Proceeds from Sales	Gross Realized Gains	Gross Realized Losses
For the year ended December 31, 2018	$ 81,681	$ 518	$ (1,611)
For the year ended December 31, 2017	$ 70,823	$ 710	$ (571)

The Company had $783 in proceeds from sales of equity securities (FHLB stock) and no associated gross realized gains or gross realized losses for the year ended December 31, 2018. There were $694 in proceeds from sales of equity securities (FHLB stock) and no associated gross realized gains or gross realized losses for the year ended December 31, 2017.

Notes to Consolidated Financial Statements (in 000's)

Net investment income is calculated as follows:

	2018		
Debt securities available for sale	Gross Investment Income	Investment Expenses	Net Investment Income
U.S. Government, agencies and authorities securities	$ 959	$ (55)	$ 904
Mortgage-backed	2,522	(145)	2,377
All other corporate bonds	5,363	(307)	5,056
Equity securities	1,236	(71)	1,165
Total	$ 10,080	$ (578)	$ 9,502

	2017		
Debt securities available for sale	Gross Investment Income	Investment Expenses	Net Investment Income
U.S. Government, agencies and authorities securities	$ 1,302	$ (68)	$ 1,234
Mortgage-backed	1,682	(87)	1,595
All other corporate bonds	5,711	(297)	5,414
Equity securities	1,142	(59)	1,083
Total	$ 9,837	$ (511)	$ 9,326

3. Fair Value

The valuation techniques required by the authoritative accounting guidance on fair value measurements are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market expectations. These two types of inputs create the following fair value hierarchy:

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 - Instruments where significant value drivers are unobservable.

When available, the Company utilizes quoted market prices to determine fair value and classify such items in Level 1. In some cases, quoted market prices are used for similar instruments in active markets and/or model-derived valuations where inputs are observable in active markets and classify such items in Level 2. When there are limited or inactive trading markets, the Company utilizes industry–standard pricing methodologies, including discounted cash flow models, whose inputs are based on management assumptions and available current market information. These items are classified in Level 3. Further, the Company relies upon independent pricing vendors to assist in valuing certain instruments.

The following section describes the valuation methodologies used by management to measure different financial instruments at fair value.

Investments in fixed maturities and equity securities:

Pricing Level 1: Values are unadjusted quoted prices for identical securities in active markets accessible at the measurement date. Holdings consist of government securities and exchange traded mutual funds.

Pricing Level 2: Valuation is based on quoted prices for similar securities in active markets, quoted prices from those willing to trade in markets that are not active, or other observable inputs. This would include any bonds priced by Securities Evaluations, Inc. ("SE")

Pricing Level 3: Valuation is derived from unobservable inputs using techniques such as broker quotes, pricing matrices and internal calculations. The Company did not hold any Level 3 securities for the years ended December 31, 2018 and December 31, 2017.

Notes to Consolidated Financial Statements (in 000's)

Priority of market value methodology:

1. Price from an independent pricing service, such as SE
2. Market price from a broker-dealer
3. Matrix pricing

All of the prices are monitored month-over-month to highlight any significant price change. Any security with a significant price change is verified using a secondary pricing source and/or verification from a broker-dealer.

The following is a summary of the inputs used in valuing the Company's assets at fair value:

	December 31, 2018	Quoted Prices (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investment in debt securities	$ 264,877	$ 36,325	$ 228,552	$ -
Investment in equity securities	55,003	54,818	185	-
Investment in money market funds	86	86	-	-
Total	$ 319,966	$ 91,229	$ 228,737	$ -

	December 31, 2017	Quoted Prices (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investment in debt securities	$ 271,968	$ 33,696	$ 238,272	$ -
Investment in equity securities	60,362	60,192	170	-
Investment in money market funds	637	637	-	-
Total	$ 332,967	$ 94,525	$ 238,442	$ -

It is the Company's policy to recognize transfers of assets between levels of the fair value hierarchy at the end of a reporting period. For the year ending December 31, 2018, there were no transfers of assets between Level 1 and Level 2 of the fair value hierarchy. No securities were transferred out of Level 2 and into the Level 3 category as a result of limited or inactive markets during 2018. The Company does not transfer out of Level 3 and into Level 2 until such time as observable inputs become available and reliable or the range of available independent prices narrow.

Notes to Consolidated Financial Statements (in 000's)

4. Deferred Policy Acquisition Costs

The deferred policy acquisition costs at December 31, 2018 and 2017 are comprised of the following:

	2018	2017
Beginning balance	$ 2,517	$ 2,639
Additional costs capitalized		
Underwriting expenses	1,465	1,584
Royalty fees (Note 7)	793	803
Premium taxes	2,014	2,018
	4,272	4,405
Less current year amortization		
Underwriting expenses	1,528	1,577
Royalty fees (Note 7)	798	836
Premium taxes	2,013	2,114
	4,339	4,527
Ending balance	$ 2,450	$ 2,517

5. Contributed Surplus

The Company has two classes of Members: Participating and Non-Participating. Participating Members are required to make a capital contribution ("reserve premium") equal to 100% of initial annual premium on Participating policies.

The reserve premium with respect to a Participating policy is required to be repaid to the Participating Member within 60 days if the Company terminates or fails to renew the policy; in all other cases, the reserve premium generally is not required to be repaid for five years after the insured cancels, terminates, or fails to renew the policy. At December 31, 2018 and 2017, $148 and $146, respectively, related to reserve premium for all such terminated policies that was included in contributed surplus. The Company recorded distributions of $2 and $0 in reserve premium to non-renewing Participating Members during the years ended December 31, 2018 and 2017, respectively.

Non-Participating Members are not required to contribute capital. Participating Members receive dividends, share in the Company's net worth, and receive a higher proportion of votes on corporate governance matters than Non-Participating Members. Of the premiums written, 30.0% and 31.7% were attributable to Non-Participating policies during the years ended December 31, 2018 and 2017, respectively.

Notes to Consolidated Financial Statements (in 000's)

6. Provision for Income Taxes

The provision for income taxes consists of the following:

	2018	2017
Current provision	$ 2,154	$ 2,763
Deferred benefit	(189)	(1,206)
Provision for income taxes	$ 1,965	$ 1,557

Set forth below is a reconciliation of the expected and actual income tax provision:

	2018	2017
Expected tax provision at 21% and 34%, respectively	$ 2,287	$ 3,542
Tax exempt income from municipal bonds	(112)	(296)
State income taxes, net of federal benefit	35	27
Dividend received deduction	(72)	(168)
Foreign tax credits	(27)	(23)
Deferred tax remeasurement	-	(1,524)
Provision to return adjustments	34	(19)
Rate differential benefit on capital loss carryback	(189)	-
Other	9	18
Actual provision for income taxes	$ 1,965	$ 1,557

The Company's expected current income tax rate decreased from 34% in 2017 to 21% in 2018 as a result of the tax rate required to be applied to taxable income based on the TCJA. Deferred income taxes were remeasured in 2017 to reflect the 21% rate as per Note 1F.

During 2018, the Company completed its TCJA analysis which had minimal impact to the effective rate. The TCJA modified how taxpayers calculate loss reserves for tax purposes which included the extention of long-tail payment patterns out to 24 years, and the use of an interest rate based upon the corporate bond yield curve. The IRS published the new discount factors based on the the new tax law in December 2018. Pursuant to the TCJA, the difference between the taxable loss reserves calculated under the old and new methods is to be spread over an eight-year period. As a result, the Company reduced its cumulative tax loss reserves balance by $2,115 which will be amortized over 8 years at a cost of $264.

The Company files a consolidated federal income tax return. Income tax provisions are allocated to the Company's wholly-owned subsidiaries as if they had been calculated on a separate company basis. State income taxes are paid by Mutual, Brokers and Services on a separate company basis. Net payments for federal income taxes were $1,250 and $3,750 in 2018 and 2017, respectively.

Notes to Consolidated Financial Statements (in 000's)

The deferred income tax amounts reflected in the Consolidated Balance Sheets at December 31, 2018 and 2017 are comprised of the following items:

	2018	2017
Net unearned premiums	$ 503	$ 532
Discounting of loss reserves	600	592
Post-retirement employee benefits	2,279	2,220
Other than temporarily impaired securities	822	897
Policyholder dividend	1,273	1,315
Other	538	301
Gross deferred tax assets	6,015	5,857
Deferred policy acquisition costs	(514)	(528)
Net unrealized gains on investments	(4,774)	(7,396)
Bond discount accretion	(80)	(106)
Gross deferred tax liabilities	(5,368)	(8,030)
Valuation allowance	-	-
Net deferred tax assets (liabilities)	$ 647	$ (2,173)

The Company believes that as of December 31, 2018, there were no material uncertain tax positions that would require disclosure under GAAP. As of December 31, 2018, the Company's 2017, 2016, and 2015 tax years were open under current Internal Revenue Service regulations and applicable state tax law and as such, potentially subject to examination.

7. Related Party Transactions

The Company is party to a royalty agreement and a services and facilities agreement with the ICI. Under the royalty agreement, Mutual is required to pay 1% of gross annual premium as a royalty fee to the ICI, limited to a total maximum of $1,000 in any calendar year. Royalty fees incurred and paid in 2018 and 2017 were $794 and $821, respectively.

The services and facilities agreement requires the Company to reimburse the ICI for actual direct and indirect expenses incurred on behalf of the Company. Service and facility fees amounted to approximately $907 and $887 for 2018 and 2017, respectively. Amounts payable at December 31, 2018 and 2017 under this agreement were approximately $76 and $222, respectively.

Years Ended December 31, 2018 and 2017 (in 000's)

8. Reinsurance Agreements

The Company utilizes reinsurance agreements to provide protection for claims in excess of the Company's normal retention limits. In addition, the Company may utilize reinsurance agreements to provide increased limits of liability on a case-by-case basis.

The Company reports ceded reinsurance balances on a gross basis. Accordingly, the following balance sheet accounts are grossed up by the amounts noted below:

	2018	2017
Reserve for losses and loss adjustment expenses	$ 83,485	$ 89,395
Unearned premiums	$ 34,231	$ 34,282

Reinsurance recoverable was mostly concentrated with St. Paul Fire & Marine Insurance Company (approximately 25%) and Lloyds of London (approximately 10%) at December 31, 2018, and St. Paul Fire & Marine Insurance Company (approximately 22%) and Lloyds of London (approximately 12%) at December 31, 2017.

Insurance risks ceded to reinsurance companies would become a liability in the event the reinsurers are unable to meet their obligations assumed under reinsurance contracts.

Premiums and losses in 2018 and 2017 have been adjusted as follows as a result of voluntary reinsurance:

	2018		2017	
Premiums	Written	Earned	Written	Earned
Direct and assumed	$ 79,264	$ 79,762	$ 80,355	$ 83,626
Ceded	(51,595)	(51,646)	(51,733)	(54,054)
Net	$ 27,669	$ 28,116	$ 28,622	$ 29,572

Losses and loss adjustment expenses	2018	2017
Direct	$ (9,120)	$ 24,636
Ceded	17,190	(13,313)
Net	$ 8,070	$ 11,323

The 2018 Direct and Ceded Losses and loss adjustment expenses amounts in the table immediately above are impacted by the $52 million claim payment return and reinsurance transfer disclosed in Note 9. Excluding this transaction, 2018 Direct and Ceded Losses and loss adjustment expenses would have been $42,441 and $(34,371), respectively, with no impact on the Net loss and loss adjustment expenses reported in the Consolidated Statement of Operations.

Notes to Consolidated Financial Statements (in 000's)

9. Reserve for Losses and Loss Adjustment Expenses

The following table sets forth a reconciliation of beginning and ending reserve for losses and loss adjustment expenses, as shown, in the Company's consolidated financial statements for the periods indicated:

	2018	2017
Balance at January 1	$ 147,299	$ 252,934
Less reinsurance recoverable, unpaid losses	(89,395)	(187,235)
Net balance at January 1	57,904	65,699
Incurred related to:		
Current year	19,700	22,995
Prior years	(11,630)	(11,672)
Total incurred	8,070	11,323
Paid related to:		
Current year	396	2,328
Prior years	11,131	16,790
Total paid	11,527	19,118
Net balance at December 31	54,447	57,904
Plus reinsurance recoverable, unpaid losses	83,485	89,395
Balance at December 31	$ 137,932	$ 147,299

As a result of changes in estimates of incurred losses related to insured events of prior years, the reserve for losses and loss adjustment expenses decreased $11,630 and $11,672 in 2018 and 2017, respectively. The decrease in 2018 was primarily the result of changes in estimates of incurred losses on D&O/E&O policies of $1,276, $3,855, and $3,150 related to insured events of 2017, 2016, and 2013, respectively. The decrease in 2017 was primarily the result of changes in estimates of incurred losses on D&O/E&O policies of $5,157, $1,003, $3,135, and $850 related to insured events of 2016, 2015, 2013, and 2010, respectively. No additional premiums or return premiums have been accrued as a result of the effects of insured events of prior years.

In the first quarter of 2017, the Company paid in excess of $100 million in claims and collected over $95 million in associated reinsurance that is included in the balance at January 1, 2017, in the table above. Subsequent claim developments resulted in a return to the Company in the fourth quarter of 2018 of approximately $52 million of such paid claim amounts. As this $52 million had previously been collected by the Company from facultative reinsurers, it was promptly transferred by the Company back to them.

The following is information about incurred and paid claims development as of December 31, 2018, net of reinsurance, as well as cumulative claim frequency, and the total of incurred-but-not-reported plus expected development on reported claims included within the reserve for net losses and loss adjustment expenses. The information about incurred and paid claims development for the years ended December 31, 2009, to 2017, is presented as unaudited supplementary information. The cumulative number of reported claims are reported as the actual individual count, not in thousands.

This information is provided on a report year basis, consistent with the nature of the policies underwritten by the Company. Specifically, the Company writes claims-made policies that cover claims reported over the policy term rather than the date of the incident giving rise to the claim. Accordingly, the cumulative number of reported claims reflect all claims received by the Company and recorded on the Company's claims bordereau by date reported.

The following development data by report year is not disaggregated by line of business or any other measure as over 90% of the Company's incurred and paid losses over the development period is derived solely from domestic D&O/E&O coverage that shares the same characteristics.

Average annual percentage payout of incurred claims by age, net of reinsurance, is also presented below.

	Incurred claims and allocated claim adjustment expenses, net of reinsurance and subrogation For Years Ended December 31,										As of December 31, 2018	
	Prior Years Unaudited										IBNR (Expected Development of Reported Claims)	Cumulative Number of Reported Claims
Report Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018		
2009	$30,000	$25,400	$23,750	$19,000	$18,350	$18,100	$17,850	$17,500	$17,300	$17,250	$ 34	26
2010		25,000	22,425	21,350	17,100	17,025	16,965	16,450	15,600	15,375	80	23
2011			21,200	18,950	17,241	15,641	14,841	14,541	14,541	14,491	1,086	54
2012				23,625	19,325	13,790	10,525	7,925	7,805	7,605	562	38
2013					17,250	14,100	11,416	9,614	6,481	3,331	838	24
2014						15,350	16,501	12,292	11,540	11,220	1,466	26
2015							24,715	27,950	26,600	26,540	1,629	69
2016								23,300	18,350	13,836	6,919	49
2017									22,970	19,700	9,262	44
2018										19,675	13,660	31
									Total	$ 149,023		

Notes to Consolidated Financial Statements (in 000's)

Cumulative paid claims and allocated claims adjustment expenses, net of reinsurance and subrogation
For Years Ended December 31,

Prior Years Unaudited

Report Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
2009	$5,078	$5,779	$15,095	$17,884	$17,515	$17,258	$17,176	$17,180	$17,187	$17,196
2010		3,356	8,138	10,239	11,247	14,242	14,225	14,225	15,229	15,230
2011			244	6,232	10,798	12,692	12,991	13,037	13,085	13,114
2012				2,015	2,512	3,558	6,510	6,533	6,565	6,569
2013					120	1,331	1,377	1,960	1,978	1,986
2014						598	1,298	2,559	5,663	8,265
2015							4,921	9,570	18,171	22,195
2016								198	4,191	5,999
2017									2,328	3,847
2018										396
									Total	$ 94,797
All outstanding liabilities before 2009, net of reinsurance										174
Liabilities for unpaid claims and claims adjustment expenses, net of reinsurance										$ 54,400

Average Annual Percentage Payout of Incurred Claims by Age, Net of Reinsurance - Unaudited

Years	1	2	3	4	5	6	7	8	9	10	11
Incremental Payout %	3.9%	33.1%	28.5%	18.9%	6.1%	4.4%	1.8%	1.7%	1.4%	0.1%	0.1%

Reconciliation of the Disclosure of Incurred and Paid Claims Development to the Liability for Unpaid Claims and Claims Adjustment Expense:

	As of December 31, 2018
Net Outstanding Liabilities	
Liabilities for Unpaid Claims and Claims Adjustment Expenses, Net of Reinsurance	$ 54,400
Unallocated Claims Adjustment Expenses	47
Total Net Liability for Unpaid Claims and Claims Adjustment Expenses	54,447
Total Reinsurance Recoverable on Unpaid Claims	83,485
Total Gross Liability for Unpaid Claims and Claims Adjustment Expenses	$ 137,932

Notes to Consolidated Financial Statements (in 000's)

10. Contingencies

In the normal course of its business activities, the Company may be subject to various asserted and unasserted claims and lawsuits covering a wide range of matters. The Company is not aware of any events that would give rise to a claim at December 31, 2018.

11. Policyholders' Dividend

In determining the level of dividend to declare, the Board of Directors ("Board") reviews the financial results of the Company as well as the anticipated capital levels needed to fund the Company's future operations and to maintain the Company's sound financial condition. After a review of all these factors, the Board declared a dividend of $6.0 million in both 2018 and 2017. $5.9 million of the total dividends declared in 2017 were paid in 2018.

The 2018 dividend will be allocated to Participating Members based equally on each Participating Member's share of the Company's net worth determined at December 31, 2018, before payment of the dividend, and the proportion of 2018 eligible gross earned premium of the Company attributable to each Participating Member. In accordance with the by-laws of the Company, dividends will only be paid to those eligible Participating Members that renew a participating policy in the year after the dividend declaration. Dividends are accounted for on the accrual basis and will be paid on or around the policy renewal date or May 15, 2019, whichever is later.

As per Title 8, Chapter 141, Section 6005 of the Vermont Statutes, the Company sought and received the approval of the Commissioner of the VDFR prior to the payment of these dividends.

12. Employee Benefit Plans

A. Retirement Plans

The Company has three retirement plans for its employees: a noncontributory defined benefit plan, a 401(k) defined contribution plan, and a supplemental employee retirement plan.

The noncontributory defined benefit plan ("the Plan") covers substantially all regular full-time employees. The Company uses a December 31st measurement date for the Plan. Plan assets consist of equity and fixed income mutual funds.

The Plan uses the Projected Unit Credit Method as the actuarial cost method and the following weighted-average assumptions to determine the benefit obligation and net periodic pension cost for the years ended December 31, 2018 and 2017:

	2018	2017
Discount rate for benefit obligation	4.25%	3.80%
Discount rate for pension cost	3.80%	4.63%

Notes to Consolidated Financial Statements (in 000's)

Expected return on plan assets	6.25%	6.25%
Rate of compensation increase	4.00%	4.00%

Plan amounts recognized in the Consolidated Balance Sheets consist of:

	2018	2017
Noncurrent assets	$ -	$ -
Current liabilities	-	-
Noncurrent liabilities	3,185	2,568
Total	$ 3,185	$ 2,568

Plan amounts recognized in accumulated other comprehensive income, net of tax, consist of:

	2018	2017
Net loss	$ 1,811	$ 1,496
Prior service cost	-	-
Total	$ 1,811	$ 1,496

Other components of the Plan for the years ended December 31, 2018 and 2017, were as follows:

	2018	2017
Projected benefit obligation	$ 12,590	$ 12,579
Fair value of plan assets	9,405	10,011
Funded status of the plan	$ (3,185)	$ (2,568)
Employer contributions	$ -	$ -
Lump sum payments	$ -	$ 813
Benefits paid	$ 31	$ 31

The Plan's accumulated benefit obligation is $9,960 as of December 31, 2018 and was $9,724 as of December 31, 2017. Pension expense for the Plan totaled $652 and $772 for the years ended December 31, 2018 and 2017, respectively, and is included in "Underwriting, general and administrative expenses" in the Consolidated Statements of Operations.

The Plan net (gain)/loss that was recognized in other comprehensive income was $73 and $(1) in 2018 and 2017, respectively. The net loss and prior service cost for the Plan that was amortized from accumulated other comprehensive income into net periodic pension expense was $108 and $0 in 2018 and $119 and $0 in 2017, respectively.

Notes to Consolidated Financial Statements (in 000's)

The Company determines the long-term expected rate of return on Plan assets by examining historical returns and the Plan's asset allocation. Factors such as inflation and current interest rates are also evaluated. The result is reviewed against benchmarking data to ensure that the return is a reasonable and appropriate assumption.

The Plan's asset allocation at December 31, by asset category, is as follows:

	2018	2017
Asset Category:		
Equities	57%	62%
Fixed income securities	43%	38%
Total	100%	100%

The Company's expected long-term rate of return and projected asset allocation are as follows:

	Expected Rate of Return	Guideline Asset Allocation	Expected Net Rate of Return
Asset Category:			
Equities	7.08%	60%	4.25%
Fixed income securities	5.00%	40%	2.00%
Total		100%	6.25%

The Plan's assets will be invested in a prudent manner for the exclusive purpose of providing benefits to Plan participants. The Company's objective is to maximize the return on assets, over the long term, by investing a majority of assets in equities. The inclusion of additional asset classes with differing rates of return, volatility, and correlation are utilized to reduce the risk by providing diversification relative to equities. The Company's investment policy states that equities will comprise 60% of assets, and fixed income securities 40% of assets. The actual allocation will be compared to the target allocation and the Plan's assets rebalanced as determined by the Company.

The Company made contributions of $0 to the Plan for both years ended December 31, 2018 and 2017, respectively. The Company's funding policy is to make annual contributions, if required, at least equal to normal costs determined to meet benefit payments, including lump sum distributions, and comply with funding requirements of ERISA. The Company does not expect to make contributions to the Plan in 2019.

The estimated net loss and prior service cost for the Plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $108 and $0, respectively.

Notes to Consolidated Financial Statements (in 000's)

Benefit payments expected to be paid from the Plan over the next five years and accumulated over the five years thereafter are as follows as of December 31:

Year	Benefits
2019	$ 1,100
2020	$ 1,420
2021	$ 290
2022	$ 350
2023	$ 380
2024-2028	$ 7,940

The 401(k) defined contribution plan covers substantially all employees. Effective January 1, 2007, the Company contributes amounts to the plan sufficient to credit each participant's account with an amount equal to 3% of the participant's eligible compensation, subject to IRS limitations, during the plan year. In addition, the Company matches 100% of the first 1% and 50% of the next 1% of employee voluntary contributions of the participant's eligible compensation. Participants are not required to contribute to the plan. Participants may voluntarily contribute up to 50% of eligible compensation paid to the participant during the plan year up to a maximum of $19. The Company contributed approximately $152 and $133 to this plan in 2018 and 2017, respectively.

The Company maintains a supplemental employee retirement plan ("SERP") which was established for certain key employees. The SERP provides benefits equal to what would be available under both the qualified non-contributory defined benefit plan and the 401(k) defined contribution plan, if there were no statutory limitations on the amount of compensation that could be covered by the qualified plans.

Defined Benefit Component:

The SERP uses the Projected Unit Credit Method as the actuarial cost method and the following weighted-average assumptions to determine the benefit obligation and net periodic pension cost for the years ended December 31, 2018 and 2017:

	2018	2017
Discount rate for benefit obligation	4.05%	3.72%
Discount rate for pension cost	3.72%	4.23%
Rate of compensation increase	4.00%	4.00%

Notes to Consolidated Financial Statements (in 000's)

SERP amounts recognized in the Consolidated Balance Sheets consist of:

	2018	2017
Noncurrent assets	$ -	$ -
Current liabilities	240	216
Noncurrent liabilities	1,694	1,595
Total	$ 1,934	$ 1,811

SERP amounts recognized in accumulated other comprehensive income, net of tax, consist of:

	2018	2017
Net loss	$ 208	$ 223
Prior service cost	-	-
Total	$ 208	$ 223

Other components of the SERP for the years ended December 31, 2018 and 2017 were as follows:

	2018	2017
Projected benefit obligation	$ 1,934	$ 1,811
Fair value of plan assets	-	-
Funded status of the plan	$ (1,934)	$ (1,811)
Employer contributions	$ -	$ -
Lump sum payments	$ -	$ 755
Benefits paid	$ -	$ -

The SERP's accumulated benefit obligation is $1,838 as of December 31, 2018 and was $1,641 as of December 31, 2017. Included in "Underwriting, general and administrative expenses" in the accompanying Consolidated Statements of Operations at December 31, 2018 and 2017, are net periodic benefit costs attributable to this plan of approximately $202 and $358, respectively.

A settlement occurred during the fiscal year ending 2017. Settlements are faily common in SERP plans that allow lump sum payments. The settlement resulted in a $144 loss to the 2017 net periodic benefit cost which was recognized in changes in other comprehensive income.

Notes to Consolidated Financial Statements (in 000's)

The SERP net (gain)/loss that was recognized in other comprehensive income was $(8) and $13 in 2018 and 2017, respectively. The net loss and prior service cost for this plan that was amortized from accumulated other comprehensive income into net periodic benefit cost was $72 and $0 in 2018 and $91 and $0 in 2017, respectively.

The Company anticipates contributing amounts equal to the benefits payable in future plan years.

The estimated net loss and prior service cost for the SERP that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $45 and $0, respectively.

Benefit payments expected to be paid from the SERP over the next five years and accumulated over the five years thereafter are as follows as of December 31:

Year	Benefits
2019	$ 240
2020	$ 1,530
2021	$ -
2022	$ -
2023	$ -
2024-2028	$ -

The accrued liability included in the Consolidated Balance Sheet for the defined contribution component of the SERP was $157 at December 31, 2018 and $141 at December 31, 2017. Amounts recognized in the Consolidated Statements of Operations for the defined contribution component of the SERP were $16 at December 31, 2018 and $15 at December 31, 2017.

B. Postretirement Benefit Plan

The Company provides health benefits to qualifying employees and retirees. The Company recognizes the expected cost of these benefits during the years in which employees render service. No assets are set aside for postretirement health benefits. The Company has not applied for benefits under the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the "2003 Act") and any measures of the accumulated postretirement benefit obligation or net periodic postretirement benefit cost in the financial statements or accompanying notes do not reflect the effects of the 2003 Act on the Company's postretirement benefit plan.

As of December 31, 2010, the Company has included a 1% load in the plan's amounts to account for the anticipated impact of the excise tax on high cost plans as a result of the Patient Protection and Affordable Care Act of 2010 (the "2010 Act"). The other provisions of the 2010 Act are not expected to have a material impact on the Company's postretirement benefit plan obligation.

Notes to Consolidated Financial Statements (in 000's)

Plan amounts recognized in the Consolidated Balance Sheets consist of:

	2018		2017	
Noncurrent assets	$	-	$	-
Current liabilities		66		65
Noncurrent liabilities		3,770		3,302
Total	$	3,836	$	3,367

Plan amounts recognized in accumulated other comprehensive income, net of tax, consist of:

	2018		2017	
Net loss	$	1,109	$	777

Other components of the plan for the years ended December 31, 2018 and 2017, were as follows:

	2018		2017	
Benefit obligation	$	3,836	$	3,367
Fair value of plan assets		-		-
Funded status of the plan	$	(3,836)	$	(3,367)
Employer contributions	$	98	$	83
Participant contributions	$	13	$	15
Benefits paid	$	111	$	98

The following table shows the plan's obligation by participant as well as assumed discount rates:

	2018		2017	
Retirees	$	(1,589)	$	(1,239)
Other active participants		(2,247)		(2,128)
Accumulated postretirement benefit obligation	$	(3,836)	$	(3,367)
Weighted average assumed discount rate to determine:				
The benefit obligation		4.25%		3.86%
The net benefit cost		3.86%		4.59%

Notes to Consolidated Financial Statements (in 000's)

Included in "Underwriting, general and administrative expenses" in the accompanying Consolidated Statements of Operations at December 31, 2018 and 2017, are net periodic benefit costs attributable to this plan of approximately $403 and $274, respectively.

The plan net (gain)/loss that was recognized in other comprehensive income was $275 and $(169) in 2018 and 2017, respectively. The net loss and prior service cost for this plan that was amortized from accumulated other comprehensive income into net periodic benefit cost was $112 and $0 in 2018 and $45 and $0 in 2017, respectively.

The Company's policy is to contribute the amount required to fund postretirement benefits as they become due to retirees. The amount expected to be required in contributions to the plan during 2019 is $66.

The estimated net loss and prior service cost for the plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $89 and $0, respectively.

Benefit payments expected to be paid from the plan over the next five years and accumulated over the five years thereafter are as follows as of December 31:

Year	Benefits
2019	$ 66
2020	$ 80
2021	$ 86
2022	$ 93
2023	$ 96
2024-2028	$ 740

For measurement purposes, a 7.5% increase in healthcare costs was assumed for fiscal year 2018, trending down to 5% in 2028 and thereafter. A 1% increase in this rate would increase the postretirement benefit obligation by $873 and the service and interest cost by $81. A 1% decrease in this rate would decrease the postretirement benefit obligation by $668 and the service cost and interest cost by $58.

C. Deferred Compensation Plan

During 2010, the Company adopted a deferred compensation plan for certain key employees. The amount and timing of awards to participants is at the sole discretion of the Company with amounts unfunded and unvested until the employee meets all of the criteria established by the Company for payment of the awarded amounts. Included in "Underwriting, general and administrative expenses" in the accompanying Consolidated Statements of Operations at December 31, 2018 and 2017 are amounts attributable to this plan of approximately $119 and $163, respectively.

Notes to Consolidated Financial Statements (in 000's)

13. Accumulated Other Comprehensive Income

Changes in the Company's accumulated other comprehensive income by component, net of tax, are as follows:

	Unrealized Gains and (Losses) on Investments	Actuarial Unrealized Gains and (Losses) on Benefit Plans	Total
Balance at December 31, 2016	$ 14,190	$ (2,904)	$ 11,286
Net unrealized gains arising during the period	8,960	115	9,075
Reclassification adjustment for (gains) losses realized in net income	(92)	293	201
Other comprehensive income	$ 8,868	$ 408	$ 9,276
Balance at December 31, 2017	$ 23,058	$ (2,496)	$ 20,562
Net unrealized losses arising during the period	(10,727)	(269)	(10,996)
Reclassification adjustment for losses realized in net income	863	231	1,094
Other comprehensive loss	$ (9,864)	$ (38)	$ (9,902)
Reclassification of deferred tax effects	4,764	(593)	4,171
Balance at December 31, 2018	$ 17,958	$ (3,127)	$ 14,831

The Company's other comprehensive (loss) income is calculated as follows:

For the Year Ended December 31, 2018	Pretax Amount	Tax Expense or Benefit	Net of Tax Amount
Net unrealized losses on investments			
Net unrealized losses arising during the period	$ (13,578)	$ (2,851)	$ (10,727)
Reclassification adjustment for losses realized in net income	1,093	230	863
Net actuarial unrealized losses on employee benefit plans			
Net unrealized losses arising during the period	(340)	(71)	(269)
Reclassification adjustment for losses realized in net income	292	61	231
Other comprehensive loss	$ (12,533)	$ (2,631)	$ (9,902)

For the Year Ended December 31, 2017	Pretax Amount	Tax Expense or Benefit	Net of Tax Amount
Net unrealized gains on investments			
Net unrealized gains arising during the period	$ 13,527	$ 4,567	$ 8,960
Reclassification adjustment for gains realized in net income	(139)	(47)	(92)
Net actuarial unrealized gains on employee benefit plans			
Net unrealized gains arising during the period	157	42	115
Reclassification adjustment for losses realized in net income	399	106	293
Other comprehensive income	$ 13,944	$ 4,668	$ 9,276

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