Checklists and illustrative financial statements for property and liability insurance companies: a financial accounting and reporting practice aid, April 1992 edition

American Institute of Certified Public Accountants. Technical Information Division

Rosemary M. Reilly
Checklists and Illustrative Financial Statements for Corporations

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Checklists and Illustrative Financial Statements for Property and Liability Insurance Companies
A FINANCIAL ACCOUNTING AND REPORTING PRACTICE AID

Edited by
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The checklists and illustrative financial statements were developed by the staff of the Technical Information Division of the AICPA as non-authoritative technical practice aids. Readers should be aware of the following:

- The checklists and illustrative financial statements are "tools" and in no way represent official positions or pronouncements of the AICPA.

- The checklists and illustrative financial statements were updated through SAS No. 66, SSARS No. 6, FASB Statement of Financial Accounting Standards No. 105, FASB Interpretation No. 38, FASB Technical Bulletin No. 90-1, AICPA Statement of Position 90-11, the AICPA Audit and Accounting Guide, Audits of Property and Liability Insurance Companies, and AICPA Practice Bulletin No. 9. The checklists and illustrative financial statements should be modified, as appropriate, for subsequent pronouncements. In determining the applicability of a pronouncement, its effective date should also be considered.

- The checklists and illustrative financial statements should be used by or under the supervision of persons having adequate technical training and proficiency in the application of generally accepted accounting principles, generally accepted auditing standards, and statements on standards for accounting and review services.

- The checklists and illustrative financial statements do not represent minimum requirements and do not purport to be all-inclusive. The referenced standard should be reviewed if clarification is desired as to whether the disclosure indicated is required or suggested, and to what extent each disclosure is relevant to the statements being presented.

Users of the checklists and illustrative financial statements are urged to refer directly to applicable authoritative pronouncements when appropriate. If you have further questions, call the AICPA Technical Hotline (see back cover). The author wishes to acknowledge the assistance of her colleague, Martin S. Safran, CPA, who served as a consultant on this project. We dedicate this edition to the memory of our friend and colleague, J. Byrne Kelly, CPA.

Susan L. Menelaides
Director
Technical Information
# Checklist and Illustrative Financial Statements for Property and Liability Insurance Companies

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INTRODUCTION

The primary purpose of the property and liability insurance business is the spreading of risks. The term risk generally has two meanings in insurance. It can mean either a peril insured against (for example, fire is a risk to which most property is exposed) or a person or property protected (for example, young drivers, who many insurance companies believe are not good risks). For a payment known as a premium, insurance companies undertake to relieve the policyholder of all or part of a risk and to spread the total cost of similar risks among large groups of policyholders.

The functions of the property and liability insurance business include marketing, underwriting (that is, determining the acceptability of risks and the amounts of the premiums), billing and collecting premiums, investing and managing assets, investigating and settling claims made under policies, and paying expenses associated with these functions.

In conducting its business, an insurance company accumulates a significant amount of investable assets. In addition to funds raised as equity and funds retained as undistributed earnings, funds accumulate from premiums collected in advance; from sums held for the payment of claims in the process of investigation, adjustment, or litigation; and from sums held for payment of future claims settlement expenses. The accumulation of these funds, their investment, and the generation of investment income are major activities of insurance companies.

Property and liability insurance companies must file an annual statement, prepared on the basis of Statutory Accounting Practice (SAP), with each state in which the companies are licensed. The primary purpose of the extensive regulatory laws enacted by the states has been the protection of the policyholders. The Annual Statements filed with the regulatory authorities are used to monitor the financial condition of insurance companies in the periods between examinations by state or zone auditors.

The following are common accounting and reporting practices by property and liability insurance companies:

- Most property and liability insurance companies use the cash-basis method of accounting for recording purposes and the accrual-basis method for reporting purposes.
- Insurance companies usually prepare non-classified balance sheets.
- The first item in the balance sheet is usually the company's investments rather than cash.
- Evaluation of loss and loss expense reserves is subjective and involves a high degree of management judgment; con-
sequently, it entails considerable audit risk for the auditor.

• Actuarial assumptions are chosen by the actuarial profession. The auditors' responsibility is to form a judgment as to whether the actuary was guided in his work by considerations consistent with generally accepted accounting principles.

• Premiums from short-duration contracts ordinarily should be recognized as revenue over the period of the contract in proportion to the amount of insurance protection provided.

• Under some insurance contracts, the period of risk differs significantly from the contract period; in these cases the premium is recognized as revenue over the period of risk in proportion to the amount of insurance protection provided.

• Acquisition costs are deferred and charged to operations in proportion to premium revenue.
Checklists—General

Many auditors and accountants find it helpful to use checklists as practice aids to prepare financial statements and reports. Some firms have developed their own checklists for internal use, and also may have specialized checklists to meet the needs of their practices, such as checklists for clients in particular industries or clients that report to the SEC. Some state CPA societies have developed checklists as practice aids which may be available to other practitioners as well as to their own members. Some commercial publishers also include checklists in certain of their publications. However, authoritative literature does not require the use of checklists, nor does it prescribe their format or content, which may vary.

Checklists typically consist of a number of brief questions or statements that are accompanied by references to Statements on Auditing Standards, Statements on Standards for Accounting and Review Services, Statements of Financial Accounting Standards, Accounting Principles Board Opinions, Accounting Research Bulletins and AICPA Statements of Position. Some checklists also include references to FASB Interpretations and Industry Audit Guides. The extent of detail included in checklists varies with the judgment of the preparers on how extensively to refer to and highlight authoritative literature without developing a checklist that is too long and unwieldy. Accordingly, checklists may serve as convenient memory aids but cannot be used as a substitute for direct reference to the authoritative literature.

Checklists usually provide for checking off or initialing each question or point to show that it has been considered. The format used in this booklet is a typical one; it provides for "yes," "no," and "not applicable" answers and presumes that remarks would be made on separate cross-referenced memorandums. Some preparers, however, prefer to include space for remarks in the body of the checklist while others prefer alternative checklist formats. For example, a checklist format may provide for the following set of answers: "not applicable," "not material," "in statements" and "in notes" (with provisions for indicating a cross-reference to the specific statement caption or note). Another format may provide for only two answers, "disclosed" and "not applicable." Firms and practitioners who develop their own checklists should adopt formats that suit their needs and preferences.

Checklists generally are accompanied by caveats that include all of the following points:

- Use of the checklists requires the exercise of individual professional judgment and likely may require some modification based on the circumstances of individual engagements.

- The checklists are not all-inclusive and are not intended to present minimum requirements.
• Users need to modify the checklists for any pronouncements issued subsequent to those mentioned in the checklist.

If widespread circulation is expected, preparers generally also stress the nonauthoritative or unofficial status of the checklists and disclaim responsibility for the way they may be used.
Financial Statements and Notes Checklist

This checklist has been developed by the staff of the Technical Information Division of the AICPA as a nonauthoritative practice aid.

Explanation of References:

AC = Reference to section number in FASB Accounting Standards - Current Text
APB = Accounting Principles Board Opinion
ARB = Accounting Research Bulletin
AU = Reference to section number in AICPA Professional Standards (vol. 1) of SAS cited
FASBI = Financial Accounting Standards Board Interpretation
FRR = SEC Financial Reporting Release
FTB = Technical Bulletin issued by the staff of the FASB
IAG = AICPA Audit and Accounting Guide, Audits of Property and Liability Insurance Companies, as of December 31, 1990
PB = AICPA Practice Bulletin
REG S-X = SEC Regulation S-X
SAB = SEC Staff Accounting Bulletin
SAS = Statement on Auditing Standards
SFAS = Statement of Financial Accounting Standards
SOP = AICPA Statement of Position

Checklist Questionnaire

General

A. Titles and References

1. Are the financial statements suitably titled? ____ ____ ____
   [SAS 62, par. 7 (AU 623.07)]

2. Does each statement include a general reference to the notes saying they are an integral part of the financial statement presentation? ____ ____ ____
   [AU 411.04 and AU 431.02]

---

1 The FASB staff issues FASB Technical Bulletins to provide guidance concerning the application of FASB Statements or Interpretations, APB Opinions, or Accounting Research Bulletins. FASB Technical Bulletins do not establish new financial accounting and reporting standards or amend existing standards.
B. Disclosure of Accounting Policies

1. Is a description of all significant accounting policies of the reporting entity presented as an integral part of the financial statements? [APB 22, par. 8 (AC A10.102)]

2. Does disclosure of significant accounting policies encompass important judgments as to appropriateness of principles concerning recognition of revenue, and allocation of asset costs to current and future periods? [APB 22, par. 12 (AC A10.105); FTB 82-1, par. 7 (AC I25.506)]

3. Does the disclosure of significant accounting policies include appropriate reference to details presented elsewhere (in the statements and notes thereto) so duplication of details is avoided? [APB 22, par. 14 (AC A10.107)]

4. For GAAP reporting purposes were the following regulatory accounting practices avoided? [IAG, p. 77]
   a. Recording bonds and stocks at carrying amounts required by the NAIC. ___ ___ ___
   b. Exclusion of nonadmitted assets from the balance sheet. ___ ___ ___
   c. Expensing of policy acquisition costs when incurred. ___ ___ ___
   d. Reporting of policyholder dividends as liabilities when declared. ___ ___ ___
   e. Recording minimum liabilities for losses based on statutory formulas. ___ ___ ___
   f. Recognition of salvage and subrogation amounts on the cash-basis. ___ ___ ___
   g. No deferred federal income taxes recorded. ___ ___ ___

5. Are the financial statements of all consolidated and unconsolidated subsidiaries presented in conformity with GAAP? [SFAS 94, par. 13 (AC C51.102); IAG, p. 91] ___ ___ ___
C. Accounting Changes

1. For all changes in accounting principle, were the following disclosures made in the year of change?
   [APB 20, pars. 17 and 19 (AC A06.113 and .115)]
   a. Nature of the change. 
   b. Justification for the change. 
   c. Effect on income before extraordinary items and on net income. 
   d. Effect on related per share amounts. 

2. For those changes in accounting principles requiring disclosure of cumulative effect and pro forma amounts, are such disclosures made? 
   [APB 20, pars. 19-21, 25 (AC A06.115-.118 and .121)]

3. For changes in the method of accounting for postretirement life insurance and health care benefits, are appropriate disclosures made? 
   [FTB 87-1, par. 4 (AC P50.503)]

4. For those changes in accounting principles requiring restatement of prior periods, is the effect of the change disclosed for all periods presented? 
   [APB 20, pars. 28 and 35 (AC A06.124 and A35.113)]

5. Were the applicable AICPA Statements of Position and Guides listed in Appendix A to SFAS 83 (AC section A06, Exhibit 112A) considered to justify a change in accounting principle? 
   [SFAS 32, pars. 10-11 (AC A06.112); APB 20, par. 16; SFAS 83, pars. 5-6 (AC A06.112)]
6. For a change in accounting estimate affecting several future periods, were the following disclosures made in the year of change? [APB 20, par. 33 (AC A06.132)]

   a. Effect on income before extraordinary items and on net income.  
      YES  NO  N/A

   b. Effect on related per share amounts.  
      YES  NO  N/A

7. Is the correction of an error shown as a prior period adjustment with disclosure of the following in the period of its discovery and correction? [APB 20, pars. 36-37 (AC A35.105)]

   a. Nature of the error in previously issued financial statements.  
      YES  NO  N/A

   b. Effect of its correction on income before extraordinary items, net income, and related per share amounts.  
      YES  NO  N/A

8. If interim financial data and disclosures are not separately reported for the fourth quarter, and an accounting change is made during the fourth quarter, is disclosure made in the year of change? [APB 28, par. 31; SFAS 3, par. 14 (AC I73 .147)]

   a. The effect on the interim periods.  
      YES  NO  N/A

   b. Cumulative effect.  
      YES  NO  N/A

D. Comparative Financial Statements

1. Have comparative statements been considered? [ARB 43, Ch. 2A, pars. 1-2 (AC F43.101-.102)]

   YES  NO  N/A

2. Are the notes and other disclosures included in the financial statements of the preceding year(s) presented, repeated, or at least referred to, to the extent that they continue to be of significance? [ARB 43, Ch. 2A, par. 2 (AC F43.102)]

   YES  NO  N/A

3. If changes have occurred in the manner of or basis for presenting corresponding items for
two or more periods, are appropriate explanations of the changes disclosed?
[ARB 43, Ch. 2A, par. 3 (AC F43.103)]

E. Business Combinations

1. If a business combination occurred during the period and met the specified conditions for a pooling of interests:
[APB 16, pars. 45-48 (AC B50.104-.107)]

   a. Was the required accounting method applied? 
   [APB 16, pars. 50-62 (AC B50.109-.121)]

   b. Do the statements and notes include the required disclosures? 
   [APB 16, pars. 63-65 (AC B50.122-.124)]

2. If a business combination does not meet the specified conditions for a pooling of interests:

   a. Was the combination accounted for by the purchase method? 
   [APB 16, pars. 66-94; SFAS 96, pars. 23 and 205c (AC B50.125-.147A and .159-.163); SFAS 38 (AC B50.148-.150 and .166); FASBI 9, pars. 4-7 (AC B50.155-.157)]

   b. Do the statements and notes include the required disclosures? 
   [APB 16, pars. 95-96 (AC B50.164-.165)]

   c. In connection with the acquisition of a banking or thrift institution, are the nature and amounts of any regulatory financial assistance disclosed? 
   [SFAS 72, par. 11 (AC B50.158F)]

3. If significant, was separate disclosure made of the amount of net operating loss or tax credit carry-forwards for which any tax benefits will be applied to reduce goodwill and other noncurrent assets (of an acquired enterprise)? 
[SFAS 96, par. 29 (AC I25.128 and .187)]

4. If financial statements for prior years are restated, were all purchase business combinations consummated in those prior years re-
measured in accordance with the requirements of SFAS 96?

[SFAS 96, par. 35]

F. Consolidations

1. If consolidated statements are presented:
   a. Is the consolidation policy disclosed?
      [ARB 51, par. 5 (AC C51.108); APB 22, par. 13 (AC A10.106)]
   b. Are intercompany balances and transactions eliminated?
      [ARB 51, par. 6 (AC C51.109)]
   c. In instances when the financial reporting periods of subsidiaries differ from that of the parent, is recognition given to the effect of intervening events that materially affect financial position or the results of operations?
      [ARB 51, par. 4 (AC C51.107); SFAS 12, pars. 18-20 (AC I89.112-.114); FASBI 13 (AC I89.120-.122)]

2. Are the accounts of majority-owned subsidiaries consolidated?
   [SFAS 94, par. 13 (AC C51.103)]

3. If the consolidated financial statements include more than one accepted practice of accounting for marketable securities, are the required disclosures for the various methods disclosed?
   [SFAS 12, par. 20 (AC I89.114)]

4. Do disclosures about formerly unconsolidated majority-owned subsidiaries financial statements for fiscal years 1986 or 1987 include summarized information about the assets, liabilities, and results of operations (or separate statements) in the consolidated financial statements or notes?
   [SFAS 94, par. 14 (AC C51.120A)]

5. Are property and liability insurance companies or property and liability holding companies, even those whose subsidiaries consist of companies engaged in diverse financial activi-
ties, consolidating all majority-owned companies unless control is considered temporary or does not rest with the majority owner?

[SFAS 94, par. 13 (AC C51.102)]

G. Related-Party Transactions and Economic Dependency

1. For related-party transactions do disclosures include:

a. The nature of the relationship(s) involved (e.g., parent, subsidiary and affiliate companies, officers, stockholders, etc.)?

[SFAS 57, par. 2 (AC R36.102)]

b. A description of the transactions, including transactions to which no amounts or nominal amounts were ascribed, for each of the periods for which income statements are presented, and such other information deemed necessary to an understanding of the effects of the transactions on the financial statements?

[SFAS 57, par. 2 (AC R36.102)]

c. The dollar amounts of transactions for each of the periods for which income statements are presented and the effects of any change in the method of establishing the terms from that used in the preceding period?

[SFAS 57, par. 2 (AC R36.102)]

d. Amounts due from or to related parties as of the date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement?

[SFAS 57, par. 2 (AC R36.102)]

e. If part of a group that files a consolidated tax return, is the amount of current and deferred tax expense disclosed for each of the periods for which income statements are presented and the amount of any tax-related balance due to or from affiliates as of the date of each balance sheet presented?

[SFAS 96, par. 30 (AC I25.129)]
f. Also, if part of a group that files a consolidated tax return, are the principal provisions of the method in which current and deferred tax expense is allocated to members of the group and the nature and effect of any changes in the method disclosed for each of the periods for which income statements are presented? ___ ___ ___ [SFAS 96, par. 30 (AC I25.129)]

2. Is information about economic dependency disclosed when necessary for a fair presentation? ___ ___ ___ [SFAS 21, par. 9 (AC S20.103)]

3. Is the nature of a controlled relationship disclosed, even though there are no transactions between the enterprises, if the reporting enterprise and one or more other enterprises are under common ownership or management control and the existence of the control could result in operating results or financial position of the reporting enterprise significantly different from those that would have been obtained if the enterprise were autonomous? ___ ___ ___ [SFAS 57, par. 4 (AC R36.104)]

H. Financial Instruments

1. Does the Company have a financial instrument that is: [SFAS 105, par. 6 (AC F25.106)]
   a. Cash in banks or on hand, or ___ ___ ___
   b. Evidence of an ownership interest in an entity, or ___ ___ ___
   c. A contract that both:
      (1) Imposes on one entity a contractual obligation (liability):
          (i) To deliver cash or financial instruments to a second entity or ___ ___ ___
          (ii) To exchange financial instruments on potentially unfavorable terms with the second entity? ___ ___ ___
(2) Conveys to that second entity a contractual right:

(i) To receive cash or another financial instrument from the first entity or

(ii) To exchange other financial instruments on potentially favorable terms with the first entity?

2. For financial instruments with off-balance-sheet risk (except for certain financial instruments specifically exempted by SFAS 105), are the following disclosed either in the body of the financial statements or in the notes by class of financial instrument? [SFAS 105, par. 17 (AC F25.112)]

a. The face or contract amount (or notional principal amount if there is no face or contract amount).

b. The nature and terms, including, at a minimum, a discussion of:

(1) The credit and market risk of those instruments.

(2) The cash requirements of those instruments.

(3) The related accounting policy pursuant to the requirements of APB 22, Disclosure of Accounting Policies.

3. For financial instruments with off-balance-sheet risk (except as noted above in H.2.), are the following disclosed either in the body

---

1 Practices for grouping and separately identifying—classifying—similar financial instruments in statements of financial position, in notes to financial statements, and in various regulatory reports, have developed and become generally accepted, largely without being codified in authoritative literature. In this Statement, class of financial instrument refers to those classifications.
of the financial statements or in the notes by class of financial instrument? [SFAS 105, par. 18 (AC F25.113)]

a. The amount of accounting loss the Company would incur if any party to the financial instrument failed completely to perform according to the terms of the contract and the collateral or other security, if any, for the amount due proved to be of no value to the entity. 

   __ __ __

b. The Company's policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the Company's access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

   __ __ __

4. Do disclosures of all significant concentrations of credit risk arising from all financial instruments, whether from individual counterparty or groups of counterparties (except for certain insurance and investment contracts, purchase and pension obligations), include:
   [SFAS 105, par. 20 (AC F25.115)]

a. Information about the (shared) activity, region, or economic characteristic that identifies the concentration?

   __ __ __

b. The amount of the accounting loss due to credit risk the Company would incur if parties to the financial instruments that make up the concentration failed completely to perform according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value to the Company?

   __ __ __

c. The Company's policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the Company's access to that collateral or other security, and the nature and a brief description of the col-
lateral or other security supporting those financial instruments?  

5. Note that the disclosures required by sections H1, 2, 3 and 4 are not applicable to insurance contracts, other than financial guarantees and investment contracts as discussed in SFAS 60.  

[SFAS 105, par. 14 (AC F25.104)]

### I. Foreign Currency

1. Is the aggregate transaction gain or loss included in net income for the period disclosed?  

[SFAS 52, par. 30 (AC F60.140)]

2. Does analysis of changes during the period in the separate component of equity for cumulative translation adjustments disclose:  

[SFAS 52, par. 31 (AC F60.141)]

   a. Beginning and ending amount of cumulative translation adjustments?  

   b. The aggregate adjustment for the period resulting from translation adjustments and gains and losses from certain hedges and intercompany balances?  

   c. The amount of income taxes for the period allocated to translation adjustments?  

   d. The amounts transferred from cumulative translation adjustments and included in the determination of net income for the period as a result of the sale, or the complete or substantially complete liquidation of an investment in a foreign entity?  

3. Are rate changes occurring after the date of the financial statements and the effects on unsettled balances related to foreign currency translations disclosed, if significant?  

[SFAS 52, par. 32 (AC F60.142)]

4. Are any foreign earnings reported in addition to amounts received in the United States disclosed, if significant?  

[ARB 43, Ch. 12, par. 5 (AC F65.102)]
5. Was disclosure of principal amounts of spot and forward exchange contracts considered?  
[SFAS 80 (AC F80)]

J. Nonmonetary Transactions

1. Are nonmonetary transactions accounted for in conformity with APB 29?  
[APB 29, pars. 18-27 (AC C11.101 and N35.105-.113)]

2. Do disclosures for nonmonetary transactions during the period include:  
[APB 29, par. 28 (AC C11.102 and N35.120); FASBI 30 (AC N35.114-.119)]

   a. Nature of the transactions?  
   ___ ___ ___

   b. Basis of accounting for the assets transferred?  
   ___ ___ ___

   c. Gains or losses recognized on the transfers?  
   ___ ___ ___

3. If stock is issued to acquire the results of a research and development arrangement, for rights to use the results, or for ownership interests in the arrangement, or a successor to the arrangement, is the stock issued accounted for at its fair value or at the value of the consideration received, whichever is more clearly evident?  
[FTB 84-1, par. 7 (AC R55.504)]

K. Contingencies and Commitments

1. Are the nature and amount of accrued loss contingencies disclosed as necessary to keep the financial statements from being misleading?  
[SFAS 5, par. 9 (AC C59.108)]

2. For loss contingencies not accrued, do disclosures indicate:  
[SFAS 5, par. 10 (AC C59.109 and .111)]

   a. Nature of the contingency?  
   ___ ___ ___

   b. Estimate of possible loss or range of loss, or a statement that such estimate cannot be made?  
   ___ ___ ___
3. Are the nature and amount of guarantees disclosed (for example, obligations under standby letters of credit, guarantees to repurchase loans that have been sold)?

[SFAS 5, par. 12 (AC C59.113); FASB 34, pars. 1-3 (AC C59.114)]

YES NO N/A

4. Are gain contingencies adequately disclosed with care to avoid any misleading implications about likelihood of realization?

[SFAS 5, par. 17 (AC C59.118)]

YES NO N/A

5. Is there adequate disclosure of commitments such as those for capital expenditures, for purchase or sale of securities under financial futures contracts, and for funding of loans?

[SFAS 5, pars. 18-19 (AC C59.120); FASB 80 (AC F80)]

L. Subsequent Events

1. Are the financial statements adjusted for any changes in estimates resulting from subsequent events that provided additional evidence with respect to conditions that existed at the date of the balance sheet?

[SFAS 5, par. 8 (AC C59.105); SAS 1, secs. 560.03-.04, 560.07 and 561.01-.09 (AU 560.03-.04, 560.07 and 561.01-.09)]

YES NO N/A

2. Are subsequent events that provide evidence with respect to conditions that did not exist at the date of the balance sheet but arose subsequent to that date adequately disclosed to keep the financial statements from being misleading?

[SFAS 5, par. 11 (AC C59.112); APB 16, par. 61 (AC B50.120) and SAS 1, secs. 560.05-.07, 560.09 and 561.01-.09 (AU 560.05-.07, 560.09 and 561.01-.09)]

YES NO N/A

M. Pension Plans

1. If there is a defined benefit plan, do disclosures include:

[SFAS 87, par. 54 (AC P16.150)]

a. A description of the plan including employee groups covered, type of benefit formula, funding policy, types of assets held
and significant nonbenefit liabilities, if any, and the nature and effect of significant matters affecting comparability of information for all periods presented?  

b. The amount of net periodic pension cost for the period showing separately the service cost component, the interest cost component, the actual return on assets for the period, and the net total of other components?  

Note: The net total of other components is the net effect during the period of certain delayed recognition provisions of SFAS 87 [AC P16]. That net total includes:

(1) The net asset gain or loss during the period deferred for later recognition (in effect, an offset or a supplement to the actual return on assets).  

(2) Amortization of the net gain or loss from earlier periods.  

(3) Amortization of unrecognized prior service cost.  

(4) Amortization of the unrecognized net obligation or net asset existing at the date of initial application of SFAS 87 [AC P16].  

c. A schedule reconciling the funded status of the plan with amounts reported in the employer's statement of financial position, showing separately?  

[SFAS 87, par. 54 (AC P16.150)]  

(1) The fair value of plan assets.  

(2) The projected benefit obligation identifying the accumulated benefit obligation and the vested benefit obligation.  

(3) The amount of unrecognized prior service cost.  

(4) The amount of unrecognized net gain or loss (including asset gains and losses
(5) The amount of any remaining unrecognized net obligation or net asset existing at the date of initial application of SFAS 87.

(6) The amount of any additional liability recognized pursuant to SFAS 87, paragraph 36 (AC P16.130).

(7) The amount of net pension asset or liability recognized in the statement of financial position pursuant to SFAS 87, paragraphs 35-36 (AC P16.129-.130) (which is the net result of combining the preceding six items).

d. The weighted-average assumed discount rate and rate of compensation increase (if applicable) used to measure the projected benefit obligation and the weighted-average expected long-term rate of return on plan assets?

[SFAS 87, par. 54 (AC P16.150)]

e. If applicable, the amounts and types of securities of the employer and related parties included in plan assets, and the approximate amount of annual benefits of employees and retirees covered by annuity contracts issued by the employer and related parties?

[SFAS 87, par. 54 (AC P16.150)]

f. If applicable, the alternative amortization method used pursuant to SFAS 87, paragraphs 26 and 33 [AC P16.120 and .127], and the existence and nature of the commitment discussed in SFAS 87, paragraph 41 [AC P16.135]?

[SFAS 87, par. 54 (AC P16.150)]

g. If more than one defined benefit plan exists:

[SFAS 87, par. 56 (AC P16.153)]

(1) Have the required disclosures above been aggregated for all of the em-
ployer's single-employer defined benefit plans or disaggregated in groups so as to provide the most useful information?

(2) Are plans with assets in excess of accumulated benefit obligations not aggregated with plans that have accumulated benefit obligations that exceed plan assets?

(3) Are disclosures for plans outside the U.S. not combined with those for U.S. plans unless those plans use similar economic assumptions?

2. If there is a defined contribution plan, do disclosures include:

a. A description of the plan(s) including employee groups covered, the basis for determining contributions, and the nature and effect of significant matters affecting comparability of information for all periods presented?

b. The amount of cost recognized during the period?
   [SFAS 87, par. 65 (AC P16.162)]

c. If the pension plan has characteristics of both a defined benefit plan and a defined contribution plan:
   [SFAS 87, par. 66 (AC P16.163)]

   (1) Is the substance of the plan to provide a defined benefit?

   (2) If answer is yes, are disclosures required for a defined benefit plan made?

3. If there is a multiemployer plan, do disclosures include:

a. A description of the multiemployer plan(s) including the employee groups covered, the type of benefits provided (defined benefit or defined contribution), and the nature and effect of significant matters affect-
b. The amount of cost recognized during the period?
[SFAS 87, par. 69 (AC P16.166)]

4. If there is a settlement or curtailment of a defined benefit pension plan, or termination benefits under such plan, do disclosures include:
[SFAS 88, par. 17 (AC P16.187)]

a. A description of the nature of the event(s)?

b. The amount of gain or loss recognized?

N. Postretirement Health Care and Life Insurance Benefits

1. Do disclosures include:
[SFAS 81, par. 6 (AC P50.102)]

a. Description of benefits and employee groups covered?

b. Description of accounting and funding policies?

c. Cost of benefits recognized during the period?

d. Effect of significant matters affecting the comparability of the costs recognized for all periods presented?
O. Futures Contracts

1. If a futures contract is designated a hedge:
   [SFAS 80, par. 4 (AC F80.104 and .404)]
   a. Does the item to be hedged expose the enterprise to price (or interest rate) risk?  
      __ __ __
   b. Does the futures contract reduce the exposure to risk and is it designated as a hedge?  
      __ __ __

2. If the futures contract hedges an anticipated transaction:  
   [SFAS 80, par. 9 (AC F80.109)]
   a. Are the significant characteristics and expected terms of the anticipated transaction identified?  
      __ __ __
   b. Is it probable that the anticipated transaction will occur?  
      __ __ __

3. If a futures contract is accounted for as a hedge, does the disclosure include:  
   [SFAS 80, par. 12 (AC F80.112)]
   a. The nature of the assets, liabilities, firm commitments, or anticipated transactions that are hedged with futures contracts?  
      __ __ __
   b. The method of accounting for the futures contract including a description of the events or transactions that result in recognition in income of changes in value of the futures contracts?  
      __ __ __

P. Troubled Debt Restructurings

1. For troubled debt restructurings, are the following disclosed by major category of loans for each balance sheet presented:  
   [SFAS 15, pars. 40-41 (AC D22.136-.137); FTBs 79-6 and 79-7 (AC D22.501-.505)]
   a. Aggregate recorded investment?  
      __ __ __
b. Gross interest income that would have been recorded if loans had been current per their original terms and had been outstanding throughout the period or since origination?

[YES NO N/A]

c. Amount of interest income included in net income?

[YES NO N/A]

d. Amounts of any commitment to lend additional funds to debtors owing restructured troubled loans?

[YES NO N/A]

2. For loans sold with recourse, are the following disclosures made:

[SFAS 77, par. 9 (AC R20.109)]

a. For each period for which an income statement is presented, the amount of proceeds?

[YES NO N/A]

b. At date of each balance sheet presented, balance of sold receivables that remains uncollected?

[YES NO N/A]

Q. Lease Finance Receivables

1. Do disclosures include:

[SFAS 13, par. 23u (AC L10.119a)]

a. Appropriate components of the net investment in the leases as of the date of each balance sheet presented?

[YES NO N/A]

b. Future minimum lease payments to be received for each of the five succeeding fiscal years as of the date of the latest balance sheet presented?

[YES NO N/A]

c. Total contingent rentals included in income for each period for which an income statement is presented?

[YES NO N/A]

2. Are leasing arrangements described?

[SFAS 13, par. 23c (AC L10.119c); for amendments of SFAS 13 see SFASs 22, 23, 27, 28, 29, 76, 77, 91, 94, 96 and 98; for interpretations see FASBIs 19, 21, 23, 24, 26 and 27; for technical bulletins see FTBs 79-10, 79-12, 79-13, 79-14, 79-15, 79-16(R), 85-3, 86-2 and 88-1]
3. Are leveraged leases appropriately accounted for and reported?  
[SFAS 13, pars. 41-47 (AC L10.143-.149)]

R. Valuation Allowances

1. Are valuation reserves for losses anticipated on assets deducted from the assets to which they relate?  
[APB 12, par. 3 (AC V18.102); IAG, p. 93]

S. Other Matters

1. If required [SFAS 21 (AC S20)], does the financial statement presentation include segment information?  
[SFAS 14 (AC S20); SFAS 24 (AC S20.109-.110); SFAS 30 (AC S20.145); and FTBs 79-4, 79-5 and 79-8 (AC S20.501-.507)]
Balance Sheet

A. Investment Securities

1. Are there separate captions for each of the following investment categories? ___ ___ ___
   a. Fixed maturities ___ ___ ___
   b. Equity securities ___ ___ ___
   c. Mortgage loans on real estate ___ ___ ___
   d. Investment real estate ___ ___ ___
   e. Policy loans ___ ___ ___
   f. Other long-term investments ___ ___ ___
   g. Short-term investments ___ ___ ___

2. Are bonds reported at amortized cost if the company has both the ability and the intent to hold the bonds until maturity? ___ ___ ___
   [SFAS 60, par. 45 (AC In6.151); IAG, p. 46]

3. Are bonds reported at market value if the enterprise is a trader in bonds? ___ ___ ___
   [SFAS 60, par. 45 (AC In6.151); IAG, p. 46]

4. If bonds are reported at market value, are temporary changes in market value recognized as unrealized gains or losses and shown, net of applicable income taxes, as a separate component of stockholders' equity? ___ ___ ___
   [SFAS 60, par. 50 (AC In6.156); IAG, p. 46]

5. Are common and nonredeemable preferred stocks reported at market value and temporary changes in market value recognized as unrealized gains and losses? ___ ___ ___
   [SFAS 60, par. 46 (AC In6.152); IAG, p. 46]

6. Are redeemable preferred stocks reported at amortized cost if the enterprise has both the ability and the intent to hold them until redemption and there is no decline in the market value other than a temporary decline? ___ ___ ___
   [SFAS 60, par. 46 (AC In6.152); IAG, p. 46]
7. Are mortgage loans which were acquired at par value reported at outstanding principal balances?  
   [SFAS 60, par. 47 (AC In6.153); IAG, p. 47]  

8. Are mortgage loans that were purchased at a discount or premium reported at amortized cost with an allowance for uncollectible amounts, if any?  
   [SFAS 60, par. 47 (AC In6.153); IAG, p. 47]  

9. Are changes in the allowance for uncollectible amounts relating to mortgage loans reported in realized gains and losses?  
   [SFAS 60, par. 47 (AC In6.153); IAG, p. 47]  

10. Are real estate investments reported at cost less accumulated depreciation and an allowance for any impairment in value?  
    [SFAS 60, par. 48 (AC In6.154); IAG, p. 47]  

11. Are changes in the allowance for any impairment in value relating to real estate investments included in realized gains and losses?  
    [SFAS 60, par. 48 (AC In6.154); IAG, p. 47]  

12. Has the Company included in the notes to the financial statements an explanation of its accounting policies for debt securities held, including the basis for classification into balance sheet captions, such as investment or trading?  
    [SOP 90-11, p. 8 (IAG, p. 257)]  

13. For each balance sheet presented, has the Company disclosed the amortized cost, estimated market values, gross unrealized gains, and gross unrealized losses for each pertinent category of debt security? Examples of such categories are the following:  
    [SOP 90-11, par. 9]  
    
    a. Debt securities issued by the U.S. Treasury and other U.S. government corporations and agencies.  
    
    b. Debt securities issued by states of the U.S. and political subdivisions of the states.
c. Debt securities issued by foreign governments and not classified as loans.  

14. For the most recent balance sheet, has the Company disclosed the amortized cost and estimated market values of debt securities due:

[SOP 90-11, par. 9]

a. In one year or less?

b. After one year through five years?

c. After five years through ten years?

d. After ten years?

B. Cash

1. Is separate disclosure made for restricted cash?

[ARB 43, Ch. 3A, par. 6 (AC B05.107)]

C. Accounts Receivable and Agents' Balances

1. Does this category include insurance premiums and agents' balances uncollected?

[IAG, p. 104]

2. Does the Company disclose hypothecation or other pledging of receivables?

[SFAS 5, pars. 18 and 19 (AC C59.120)]

D. Reinsurance Recoverable on Paid Losses

1. Does this category include amounts that are recoverable from reinsurers and that relate to paid claims and claim adjustment expenses, with an allowance for estimated uncollectible amounts?

[SFAS 60, par. 38 (AC In6.144); IAG, p. 54]

2. Are the nature and significance of reinsurance transactions to the enterprise's operations, including reinsurance premiums assumed and
ceded, and estimated amounts that are recoverable from reinsurers and that reduce the liabilities for unpaid claims and claim adjustment expenses disclosed?

[SFAS 60, par. 60(f) (AC In6.166(f)); IAG, p. 54]

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3. Does the Company treat fronting arrangements as reinsurance arrangements for purposes of disclosures required by SFAS 60?

[PB, par. 6]

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E. Deferred Acquisition Costs

1. Has the Company disclosed the following relating to deferred acquisition costs?

[SFAS 60, par. 60c (AC In6.166c)]

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2. Has the Company disclosed whether it considers anticipated investment income in determining if a premium deficiency relating to short-duration contracts exists?

[SFAS 60, par 60e (AC In6.166e)]

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F. Property and Equipment

1. Has the Company disclosed the basis of determining amounts?

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2. For depreciable assets, has the Company disclosed the following?

[APB 12, par. 5 (AC D40.105)]

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d. A general description of the method or methods used in computing depreciation with respect to major classes of depreciable assets.

YES NO N/A

3. Does the Company disclose any pledged, mortgaged, or liened assets?
   [SFAS 5, pars. 18 and 19 (AC C59.120)]

YES NO N/A

4. For any accounting period in which interest costs have been capitalized, has the total amount of interest cost incurred during the period and the amount thereof that has been capitalized been disclosed?
   [SFAS 34, par. 21 (AC I67.118)]

YES NO N/A

G. Lessee Leases

1. Is the following information disclosed with respect to capital leases?
   [SFAS 13, par. 13 (AC L10.112)]

   a. The gross amount of assets recorded under capital leases as of the date of each balance sheet presented by major classes according to nature or function. This information may be combined with the comparable information for owned assets.

   YES NO N/A

   b. Future minimum lease payments as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years, with separate deductions from the total for the amount representing executory costs, including any profit thereon, included in the minimum lease payments and for the amount of the imputed interest necessary to reduce the net minimum lease payments to present value.

   YES NO N/A

   c. The total of minimum sublease rentals to be received in the future under noncancelable subleases as of the date of the latest balance sheet presented.

   YES NO N/A

   d. Total contingent rentals actually incurred for each period for which an income statement is presented.

   YES NO N/A
e. Has the Company separately identified:

(1) Assets recorded under capital leases?  __  __  __

(2) Accumulated amortization of capital leases?  __  __  __

(3) Obligations under capital leases?  __  __  __

(4) Amount of amortization of capital lease assets or the fact that the amortization of capital lease assets is included in depreciation expense?  __  __  __

2. Have the following been disclosed for operating leases having initial or remaining non-cancelable lease terms in excess of one year?

a. Future minimum rental payments required as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years.  __  __  __

b. The total of minimum rentals to be received in the future under noncancelable subleases as of the date of the latest balance sheet presented.  __  __  __

3. For all operating leases, has the Company disclosed:

[SFAS 13, par. 16 (AC L10.112)]

a. Rental expense for each period for which an income statement is presented, with separate amounts for minimum rentals, contingent rentals, and sublease rentals? (Rental payments under leases with terms of a month or less that were not renewed need not be included.)  __  __  __

b. A general description of the lessee's leasing arrangements including, but not limited to, the following:

(1) The basis on which contingent rental payments are determined?  __  __  __

(2) The existence and terms of renewal or purchase options and escalation clauses?  __  __  __
(3) Restrictions imposed by lease agreements, such as those concerning dividends, additional debt, and further leasing?

H. Other Assets

1. Consider stating as a separate line item if material.

2. Are net charges arising from financing-type reinsurance arrangements treated as deferred charges or receivables by the assuming company? [IAG, p. 55]

I. Policy Liabilities

1. Is the basis for estimating the liabilities for unpaid claims and claim adjustment expenses disclosed? [SFAS 60, par. 60a (AC In6.166a)]

2. Is the carrying amount of liabilities for unpaid claims and claim adjustment expenses relating to short-duration contracts that are presented at present value in the financial statements, and the range of interest rates used to discount those liabilities, disclosed? [SFAS 60, par. 60d (AC In6.166d)]

3. Is an unearned premium reserve presented as a liability for the portion of premiums applicable to the unexpired periods of policies? [IAG, p. 28]

4. Is the nature and significance of reinsurance transactions to the insurance companies' operations, including reinsurance premiums assumed and ceded, and estimated amounts that are recoverable from reinsurers and that reduce the liabilities for unpaid claims and claim adjustment expenses disclosed? [SFAS 60, par 60f (AC In6.166f)]

J. Income Taxes (Assumes the adoption of FASB 96)

1. Were deferred tax assets recognized for the net tax benefit of net deductible amounts that
could be realized by loss carryback from future years:
[SFAS 96, par. 17e (AU I25.116e)]

a. To reduce a current deferred tax liability? YES NO N/A

b. To reduce taxes paid in the current or a prior year? YES NO N/A

2. Were deferred tax assets or liabilities adjusted for the effect of a change in tax law or rates with the effect included in income from continuing operations for the period that includes the enactment date?
[SFAS 96, par. 20 (AC I25.11)]

YES NO N/A

3. Were deferred tax assets or liabilities attributable to different tax jurisdictions presented separately and not offset?
[SFAS 96, par. 24 (AC I25.123)]

YES NO N/A

4. Were the types of temporary differences that give rise to significant portions of a deferred tax asset or liability disclosed?
[SFAS 96, par. 24 (AC I25.123)]

YES NO N/A

5. Is the amount of a deferred tax asset or liability the net deferred tax consequence of:
[SFAS 96, par. 24 (AC I25.123)]

a. Temporary differences that will result in net taxable or deductible amounts during the next year? YES NO N/A

b. Temporary differences related to an asset or liability that is classified for financial reporting as current because of an operating cycle that is longer than one year? YES NO N/A

c. Temporary differences for which there is no related identifiable asset or liability for financial reporting [SFAS 96, par. 12 (AC I25.111)] whenever other related assets and liabilities are classified as current because of an operating cycle that is longer than one year? YES NO N/A
6. Were deferred tax liabilities recognized for temporary differences that will result in net taxable amounts in future years?  
[SFAS 96, par. 17f-h (AC I25.116f-h)]

7. For undistributed earnings of subsidiaries or corporate joint ventures, for which a deferred tax liability is not recognized, do the disclosures include:  
[SFAS 96, par. 25 (AC I25.124)]

   a. A description of the types of temporary differences?  
   b. The types of events that would cause the temporary differences to become taxable?  
   c. The cumulative amount of each type of temporary difference?  
   d. The amount of the unrecognized deferred tax liability, if determination of that liability is practicable, or a statement that determination is not practicable and the amount of withholding taxes that would be payable upon remittance of the earnings?

K. Income Taxes (APB 11)

1. Has the Company disclosed the following relating to income taxes calculated under APB 11?  
[SFAS 60, par. 60i (AC I25.124)]

   a. The treatment of policyholders' surplus under the U.S. Internal Revenue Code and that income taxes may be payable if the Company takes certain specified actions, which should be appropriately described.  
   b. The accumulated amount of policyholders' surplus for which income taxes have not been accrued.

2. Has the Company disclosed any retained earnings in excess of policyholders' surplus on which no current or deferred federal income tax provisions have been made and the reasons for not providing the deferred taxes?  
[SFAS 60, par. 60j (AC I25.125)]
L. Long-Term Debt

1. Are the major components of debt disclosed on the face of the balance sheet or in the notes? ___ ___ ___ 
   [SFAS 47, par. 10 (AC C32.105)]
   a. Is there disclosure of the aggregate amount of maturities and sinking fund requirements for all long-term borrowings and redeemable preferred stock for each of the five years following the balance sheet date? ___ ___ ___

2. Are conversion features appropriately accounted for and disclosed? ___ ___ ___ 
   [APB 14, par. 12 (AC D10.103); APB 15, par. 19 (AC E09.110)]

3. For troubled debt restructuring occurring during the current period, do disclosures include: 
   [SFAS 15, par. 25 (AC D22.121)]
   a. Description of the principal changes in terms, the major features of settlement, or both? ___ ___ ___
   b. Aggregate gain on restructuring of payables and the related income tax effect? ___ ___ ___
   c. Aggregate net gain or loss on transfers of assets recognized during the period? ___ ___ ___
   d. Per share amount of the aggregate gain on restructuring of payables, net of related income tax effect? ___ ___ ___

4. For periods after a troubled debt restructuring, do disclosures include: 
   [SFAS 15, par. 26 (AC D22.122)]
   a. Extent to which amounts contingently payable are included in the carrying amount of restructured payables? ___ ___ ___
   b. Total amounts that are contingently payable, if applicable, and conditions under which those amounts would become payable or forgiven? ___ ___ ___
5. Was debt considered extinguished for financial reporting purposes if:
(SFAS 76, par. 3 (AC D14.102A))

a. The debtor is legally released from being the primary obligor and it is probable that the debtor will not be required to make future payments with respect to the debt under any guarantee? ___ ___ ___

b. The debtor irrevocably places cash or other assets in a trust to be used solely for satisfying scheduled payments of both interest and principal of a specific obligation and the possibility that the debtor will be required to make future payments with respect to that debt is remote? ___ ___ ___

6. If there was an extinguishment of debt, was the difference between reacquisition price and carrying amount:

a. Recognized currently in income? ___ ___ ___
   (APB 26, pars. 20-21 (AC D14.103-.104); FTB 80-1, pars. 3-4 (AC D14.503-.504); SFAS 84, par. 5 (AC D14.101))

b. Identified as a separate or extraordinary item? ___ ___ ___
   (SFAS 4, par. 8 as amended by SFAS 64, par. 4 (AC D14.105))

7. Do disclosures for extinguishments of debt described in 6 above include:
(SFAS 4, par. 9 (AC D14.107))

a. Description of the extinguishment transactions, including the source of any funds used to extinguish debt if it is practicable to identify the sources? ___ ___ ___

b. Income tax effect in the period of extinguishment? ___ ___ ___

c. The per share amount of the aggregate gain or loss net of related income tax effect? ___ ___ ___

8. If debt was considered extinguished per SFAS 76, paragraph 3c, does the disclosure include:
(SFAS 76, par. 6 (AC D14.108))

35
a. A general description of the transaction?  

b. The amount of debt that is considered extinguished as long as the debt remains outstanding?  

M. Other Liabilities  

1. Are estimated losses from loss contingencies accrued if both "probable" [as explained in SFAS 5 (AC C59)] and the amount can be reasonably estimated?  

[SFAS 5, par. 8 (AC C59.105); FASBI 14 (AC C59.106-.107 and .124-.127)]  

2. Are liabilities appropriately accrued and reported for employees' compensation for future absences?  

[SFAS 43, par. 6 (AC C44.104)]  

3. Are liabilities for special termination benefits to employees appropriately accrued and reported when the employees accept the offer and the amount can be reasonably estimated?  

[SFAS 88, par. 15 (AC P16.185)]  

4. For loans transferred with recourse which are not reported as sales, is the amount of proceeds from the transfer reported as a liability?  

[SFAS 77, par. 8 (AC R20.109)]  

5. Are net credits arising from financing-type reinsurance agreements treated as a deferred credit or liability by the ceding company?  

[IAG, p. 92]  

N. Capital Stock  

1. For each class of stock, do disclosures include the number of shares authorized, issued and outstanding, and par or stated value per share?  

[APB 12, par. 10 (AC C08.102)]  

2. Do the financial statements include a description, in summary form, sufficient to explain the pertinent rights and privileges of the
various securities outstanding, for example: dividend and liquidation preferences, participation rights, call prices and dates, conversion or exercise prices and pertinent dates, sinking fund requirements, or unusual voting rights?

[APB 15, par. 19 (AC E09.110)]

3. Are the amounts of redemption requirements for all issues of capital stock redeemable at fixed or determinable prices on fixed or determinable dates disclosed for each of the five years following the date of the latest balance sheet presented?

[SFAS 47, par. 10 (AC C32.105)]

4. Are liquidation preferences of preferred stock issued disclosed in the equity section of the balance sheet in the aggregate?

[APB 10, par. 10 (AC C16.101)]

5. For preferred stock, do disclosures include:

[APB 10, par. 11 (AC C16.102)]

   a. The aggregate or per share amounts at which shares may be called or are subject to redemption?

   b. The aggregate and per share amounts of arrearages in cumulative preferred dividends?

6. For stock option and stock purchase plans, do disclosures include:

[APB 43, Ch. 13B, par. 15 (AC C47.123); FASBI 28 (AC C47.119-.122 and .138-.146); FTB 82-2, pars. .10-.12 (AC C47.513-.515); FASBI 38 (AC C47.135A-.135E)]

   a. The number of shares under option?

   b. The option price?

   c. The number of shares as to which options are exercisable?

   d. For shares exercised, the number of shares exercised and option price?
O. Retained Earnings

1. Are significant restrictions on the use of retained earnings for payment of dividends disclosed?  
   [SFAS 5, par. 18 (AC C59.120)]

2. Are any appropriations of retained earnings for loss contingencies clearly identified and included in stockholders' equity?  
   [SFAS 5, par. 15 (AC C59.117)]

3. After completion of a quasi reorganization, is a new retained earnings account established and dated with the date being disclosed in subsequent financial statements until it is no longer deemed significant?  
   [ARB 43, Ch. 7A, par. 10 (AC Q15.111); ARB 46 (AC Q15.111)]

P. Other Stockholders' Equity Accounts

1. Are cumulative translation adjustments separately disclosed?  
   [SFAS 52, par. 31 (AC F60.141)]

2. For treasury shares purchased at a stated price significantly in excess of current market price, are the allocation of amounts paid and the accounting treatment for such amounts disclosed?  
   [FTB 85-6, par. 3 (AC C23.501-.503)]

3. Is the valuation allowance for marketable equity securities separately disclosed?  
   [SFAS 12, par. 11 (AC I89.104)]

4. Do the stockholders' equity accounts include:  
   [IAG, p. 93]

   a. Capital stock (including disclosure of all pertinent data)?

   b. Capital in excess of par?

   c. Retained earnings, showing restricted and unrestricted amounts separately?

   d. Unrealized investment gains and losses?
5. If statutory surplus is below the minimum required by law, is disclosure of the relevant facts made? [IAG, p. 112]  

6. Is the following information relating to stockholders' equity, statutory capital and surplus, and the effects of statutory accounting practices on the ability to pay dividends to stockholders disclosed? [SFAS 60, par. 60h (AC In6.166h)]  

a. The amount of statutory capital and surplus.  

b. The amount of statutory capital and surplus necessary to satisfy regulatory requirements (based on current operations) if significant in relation to the statutory capital and surplus.  

c. The nature of statutory restrictions on the payment of dividends and the amount of retained earnings that is not available for the payment of dividends to stockholders.
Income Statement

A. Premium Revenue

1. Do premium balances include reinsurance premiums assumed and deduct reinsurance premiums ceded? ___ ___ ___
   [SFAS 60, par. 60(f)]

B. Investment Income

1. Is amortization of deferred loan origination, commitment, and other fees and costs recognized as an adjustment of yield, reported as interest income? ___ ___ ___
   [SFAS 91, par. 22 (AC L20.121)]

2. Except as specified in SFAS 91, paragraph 20 [AC L20.119], is the interest method used as the method of amortization? ___ ___ ___
   [SFAS 91, par. 18 (AC L20.117)]

3. Is investment income presented net of investment expenses? ___ ___ ___
   [IAG, p. 106]

4. Are realized gains and losses on all investments (except for those that are accounted for as hedges as described in SFASs 52 and 80) reported in the statement of earnings as a component of other income, on a pretax basis? ___ ___ ___
   [SFAS 97, par. 28 (AC In6.156)]

C. Other Income

1. Is amortization of loan fees being amortized on the straight-line basis over the commitment period or included in income when the commitment expires, reported as other income? ___ ___ ___
   [SFAS 91, par. 22 (AC L20.121)]

2. Are gains/losses on pension plan settlements or curtailments or termination benefits disclosed? ___ ___ ___
   [SFAS 88, par. 17 (AC P16.187)]

3. For investments in common stock accounted for by the equity method:
a. Are intercompany profits and losses appropriately eliminated until realized by the investor through transactions with independent third parties?  
[APB 18, par. 19a (AC I82.109a)]

b. Is the investor's share of earnings shown as a single amount except for investee extraordinary items and prior period adjustments that are material to the investor?  
[APB 18, pars. 19c and 19d (AC I82.109c and .109d)]

c. Are income taxes of the investor's share of the investee's earnings appropriately accrued?  
[APB 24, pars. 7-10 (AC I42.114-.116 and .119); FASBI 29 (AC I42.117-.118)]

D. Benefits and Expenses

1. Compensation:

a. If there is a compensatory stock issuance plan:

(1) Is compensation expense accrued in the proper periods?  
[APB 25, pars. 12-15 (AC C47.112-.115); FASBI 38, pars. 2-6 (AC C47.135A-.135E)]

(2) Are deferred income taxes recorded to recognize temporary differences between accrual of compensation expense and deduction for income tax purposes?  
[APB 25, pars. 16-18 (AC C47.116-.118); FTB 82-2, pars. 8 and 13 (AC C47.511 and .516)]

b. For deferred compensation agreements, are estimated amounts to be paid properly accrued?  
[APB 12, pars. 6-7 (AC C38.101-.102)]

2. Employee Benefits:

a. Is the amount of net periodic pension costs and their components disclosed?  
[SFAS 87, par. 54b (AC P16.150b)]
b. Is the cost of postretirement health care and life insurance benefits disclosed? [SFAS 81, par. 6c (AC P50.102c)]

3. Is the cost of the pension plan(s) accounted for in conformity with SFAS 87, paragraphs 20-34, 39-53 and 77? [SFAS 87, pars. 20-34, 39-53 and 77 (AC P16.114-.128, .133-.138 and .141-.149)]

4. Have settlements of defined benefit pension plans been accounted for in accordance with SFAS 88, paragraphs 3-5 and 9-11? [SFAS 88, pars. 3-5 and 9-11 (AC P16.172, .177-.179 and .181)]

5. Have curtailments of defined benefit pension plans been accounted for in accordance with SFAS 88, paragraphs 6 and 12-14? [SFAS 88, pars. 6 and 12-14 (AC P16.173 and .182-.184)]

a. Have such settlements and curtailments been properly differentiated in accordance with SFAS 88, paragraphs 7-8? [SFAS 88, pars. 7-8 (AC P16.174-.175)]

6. Have termination benefits been accounted for in accordance with SFAS 88, paragraph 15? [SFAS 88, par. 15 (AC P16.185)]

7. Has the gain or loss measured in accordance with SFAS 88, paragraphs 9-10, 12-13 or 15 (which is directly related to a disposal of a segment of a business) been included in determining the gain or loss associated with that event, and recognized in accordance with APB 30? [SFAS 88, pars. 9-10, 12-13 and 15 (AC P16 .177, .179, .182-.183 and .185)]

1 Accounting for defined contribution plans and for multi-employer plans is generally the same as current practice. The pension rules apply primarily to companies offering defined benefit pension plans.
8. Is depreciation expense for the period(s) disclosed accompanied by a general description of the method(s) used to compute depreciation for the major classes of depreciable assets?
   [APB 12, par. 5 (AC D40.105)]

   YES NO N/A

9. Is the amount of interest cost incurred disclosed in the statements or notes thereto, and for an accounting period in which some interest cost is capitalized, the total amount thereof that has been capitalized?
   [SFAS 34, par. 21 (AC I67.118)]

   YES NO N/A

10. Is discount or premium on notes receivable and payable amortized to result in a constant rate of interest when applied to the amount outstanding at the beginning of any given period (the interest method) and reported as interest?
    [APB 12, pars. 16-17 (AC I69.108); APB 21, pars. 15-16 (AC I69.108-.109)]

11. Are amounts of loan origination, commitment, and other fees and costs recognized as an adjustment of yield reported as part of interest income?
    [SFAS 91, par. 22 (AC L20.122)]

12. Is amortization of other fees, such as commitment fees that are being amortized on a straight-line basis over the commitment period or included in income when the commitment expires, reported as service fee income?
    [SFAS 91, par. 22 (AC L20.122)]

13. For sales of real estate, other than retail land sales, is revenue recognized on the full accrual basis only if all the conditions in SFAS 66, paragraph 5 are met?
    [SFAS 66, par. 5 (AC Re1.105)]

   YES NO N/A

E. Income Taxes (Assumes the adoption of SFAS 96)

1. If the Company is a public company that is not subject to income taxes because its income is taxed directly to its owners, has this fact and the net difference between the tax bases and the reported amounts of the Company's assets and liabilities been disclosed?
   [SFAS 96, par. 24 (AC I25.123)]
2. Has the amount of income tax expense or benefit been allocated to:
[SFAS 96, par. 26 (AC I25.125)]

a. Continuing operations?  

b. Discontinued operations?  

c. Extraordinary items?  

d. Cumulative effect of accounting changes?  

e. Prior period adjustments?  

f. Gains and losses included in comprehensive income but excluded from net income?  

g. Capital transactions?  

3. Were the following significant components of income tax expense attributable to continuing operations for each year presented disclosed in the financial statements or notes thereto?  
[SFAS 96, par. 27 (AC I25.126)]

a. Current tax expense or benefit.  

b. Deferred tax expense or benefit exclusive of (f) below.  

c. Investment tax credits.  

d. Government grants (to the extent recognized as a reduction of income tax expense).  

e. The benefits of operating loss carry-forwards.  

f. Adjustments of a deferred tax liability or asset for enacted changes in tax laws or rates or a change in the tax status of the enterprise.  

4. Do disclosures regarding income tax expense attributable to continuing operations include:
[SFAS 96, par. 28 (AC I25.127)]

a. A reconciliation (using percentages or dollar amounts) to the amount of income tax expense that would result from applying
domestic federal statutory tax rates to pretax income from continuing operations? ___ ___ ___

b. The estimated amount and the nature of each significant item? ___ ___ ___

5. Have the amounts and expiration dates (or a reasonable aggregation of expiration dates) of operating loss and tax credit carryforwards for financial reporting (that is, amounts not already recognized as reductions of a deferred tax liability) and for tax purposes (that is, amounts available to reduce taxes payable on tax returns in future years) been disclosed? [APB 2, par. 16, SFAS 96, par. 29 (AC I25.128 and .187)]

6. Do the disclosures for investment tax credits include the method followed (flow-through or deferral) and the amounts involved? [APB 4, par. 11 (AC I25.186)]

7. If the Company is part of a group that files a consolidated tax return, have the following items been disclosed in its separately issued financial statements? [SFAS 96, par. 30 (AC I25.129)]

   a. The amount of current and deferred tax expense for each income statement presented and the amount of any tax-related balances due to or from affiliates as of the date of each balance sheet presented. ___ ___ ___

   b. The principal provisions of the method by which the consolidated amount of current and deferred tax expense is allocated to members of the group and the nature and effect of any changes in that method (and in determining related balances to or from affiliates) during the years for which the disclosures in (a) above are presented. ___ ___ ___

8. For the earliest year restated or for the year SFAS 96 is first adopted if no prior year is restated, was the effect of applying SFAS 96 on the amount of deferred tax charges or credits at the beginning of the fiscal year reported as the effect of a change in accounting principle in a manner similar to the cumula-
tive effect of a change in accounting principle as described in APB 20, paragraph 20, Accounting Changes, except for any effects of the type required by SFAS 96 to be excluded from net income? [SFAS 96, par. 33]

9. When initially presented, did the financial statements for the year SFAS 96 was first adopted disclose the following: [SFAS 96, par. 34]

a. The effect of adopting SFAS 96 on income from continuing operations, income before extraordinary items, and net income for the year of adoption if restated financial statements for the prior year are not presented?

b. The effect of any restatement on any income from continuing operations, income before extraordinary items, and net income for each year presented?

F. Income Taxes (APB 11)

1. Are the components of income tax expense disclosed (tax expenses estimated to be currently payable, tax effects of timing differences, and tax effects of operating losses) and allocated to:
   [APB 11, par. 60 (AC I28.106)]

a. Income before extraordinary items?

b. Extraordinary items?

2. Are tax benefits realized from operating loss carryforwards (other than preacquisition losses of acquired subsidiaries) reported as an extraordinary item in the period realized? [APB 11, par. 61 (AC I17.116)]

3. Do disclosures regarding income taxes include:
   [APB 11, par. 63 (AC I28.109; SFAS 31, par. 7 (AC I42.133); TB 82-1, par. 5 (AC I28.511)]

a. Amounts of any unused operating loss carryforwards together with expiration dates (including separate identification of
amounts that upon recognition would be credited to deferred taxes)?

YES NO N/A

b. Significant amounts of any other unused deductions and/or credits together with expiration dates?

YES NO N/A

c. Reasons for variations in the customary relationships between income tax expense and pretax accounting income?

YES NO N/A

d. Domestic and foreign components of income taxes?

YES NO N/A

4. For undistributed earnings of a subsidiary and/or corporate joint venture, for which income taxes have not been accrued, do disclosures include:

[APB 23, pars. 14 and 18 (AC I42.109 and .112)]

a. Declaration of either intention to reinvest such earnings to support the conclusion that their remittance has been indefinitely postponed, or that the undistributed earnings will be remitted in the form of a tax-free liquidation?

YES NO N/A

b. Cumulative amount of undistributed earnings on which the parent company has not recognized income taxes?

YES NO N/A

5. Is the accumulated amount of bad debt reserves for which income taxes have not been accrued disclosed?

[APB 23, par. 24 (AC I42.124)]

YES NO N/A

G. Discontinued Operations

1. Are operations of a discontinued segment or one that is the subject of a formal plan for disposition:

[APB 30, pars. 8 and 13-18 (AC I13.101-103, .105-.106 and .108-.109)]

a. Reported separately from income from continuing operations and as a component (including applicable income taxes) of income before extraordinary items?

YES NO N/A
b. Accompanied by disclosure in the notes of revenue applicable to the discontinued operations? [APB 30, par. 8 (AC I13.105)]

2. Is gain or loss from disposal of a discontinued segment reported separately (including applicable income taxes) in conjunction with results of discontinued operations as a component of income before extraordinary items? [APB 30, pars. 8 and 13-18 (AC I13.101-.103, .105-.106 and .108-.109)]

3. If the Company sells part of its ownership interest in a foreign entity, is a pro rata portion of the accumulated translation adjustment component of equity attributable to that investment recognized in measuring the gain or loss on the sale? [FASBI 37, par. 2 (AC F60.120)]

4. For the period encompassing the measurement date, do notes to financial statements disclose: [APB 30, par. 18 (AC I13.108-.109)]
   a. Identity of the segment discontinued? YES NO N/A
   b. Expected disposal date, if known? YES NO N/A
   c. Expected manner of disposal? YES NO N/A
   d. Description of the remaining assets and liabilities of the discontinued segment at the balance sheet date? YES NO N/A
   e. Income or loss from operations and any proceeds from disposal of the discontinued segment during the period from the measurement date to the balance sheet date? YES NO N/A

5. For periods after measurement date and including the period of disposal, do notes to financial statements disclose the information required by 4 a. to d. above and the information required by 4 e. above compared with prior estimates? [APB 30, par. 18 (AC I13.108-.109)]
H. Extraordinary Items

1. Do extraordinary items meet both criteria of (1) an unusual nature, and (2) infrequency of occurrence?  
[APB 30, pars. 19-24 (AC I17.106-.111 and .118)]

2. Are extraordinary items segregated and shown (including applicable income taxes) following income before extraordinary items and before net income?  
[APB 30, pars. 10-12 (AC I17.102-.103)]

3. Are descriptive captions and amounts (including applicable income taxes) presented for individual extraordinary events or transactions, preferably on the face of the income statement?  
[APB 30, par. 11 (AC I17.102)]

4. Do disclosures include descriptions of an extraordinary event(s) or transaction(s) and the principal items entering into determination of extraordinary gain(s) or loss(es)?  
[APB 30, par. 11 (AC I17.102)]

5. Are material events or transactions that are either unusual in nature, or of infrequent occurrence but not both (and therefore not meeting criteria for extraordinary items):  
[APB 30, par. 26 (AC I22.101); FTB 82-1, par. 6 (AC I25.505)]

   a. Reported as a separate component of income from continuing operations?  
   [YES NO N/A]

   b. Accompanied by disclosure of the nature and financial effects of each event?  
   [YES NO N/A]

6. For gains or losses from extinguishment of debt classified as extraordinary items, do disclosures include:  
[SFAS 4, par. 9 (AC I17.104)]

   a. Description of the extinguishment transactions, including the sources of any funds used to extinguish the debt if it is practicable to identify the sources?  
   [YES NO N/A]
b. Income tax effect in the period of extinguishment?  

NO

YES

N/A

c. Per share amount of the aggregate gain or loss net of related income tax effect?  

NO

YES

N/A

I. Other

1. Are the following excluded from determination of net income or results of operations under all circumstances?  
[APB 9, par. 28 (AC C08.101)]

a. Adjustments or charges or credits resulting from transactions in the Company's own capital stock.  

NO

YES

N/A

b. Transfers to and from accounts properly designated as appropriated retained earnings.  

NO

YES

N/A

c. Adjustments made pursuant to a quasi reorganization.  

NO

YES

N/A

2. Is earnings per share information presented on the face of the income statement accompanied by appropriate disclosure that includes the basis of the calculation?  
[APB 15 (AC E09); APB 20, pars. 19c, 33, 35 and 37 (AC A06.115c and .132, A35.105 and .113); APB 30, pars. 9 and 12 (AC E09.104, I13.107 and I17.103); FASBI 31 (AC E09.128-.131 and .169-.176); FASBI 38, par. 7 (AC E09.130A); and SFAS 85, par. 3 (AC E09.123A)]

NO

YES

N/A

Statement of Changes in Stockholders' Equity

A. Are changes in separate component accounts of stockholders' equity disclosed?  
[APB 12, par. 10 (AC C08.102)]

NO

YES

N/A

B. Are changes in the number of shares of equity securities disclosed?  
[APB 12, par. 10 (AC C08.102)]

NO

YES

N/A

C. Are prior period adjustments limited to:

1. Correction of an error(s) in financial statements of prior periods?  
[SFAS 16, par. 11 (AC A35.103)]

NO

YES

N/A
2. Adjustments resulting from realization of income tax benefits of preacquisition operating loss or tax credit carryforwards of purchased subsidiaries?  
[SFAS 96, par. 23 (AC I25.122)]

YES NO N/A

D. Are prior period adjustments and their resulting effects (both gross and net of applicable income taxes) appropriately disclosed?  
[APB 9, par. 26 (AC A35.107)]

YES NO N/A

E. For a correction of an error, are the following disclosed in the period in which the error was discovered and corrected?  
[APB 20, par. 37 (AC A35.105)]

1. Nature of the error in previously issued financial statements.

YES NO N/A

2. Effect of its correction on income before extraordinary items, net income, and related per share amounts (if applicable).

YES NO N/A

Statement of Cash Flows

A. Is a statement of cash flows presented as a basic financial statement for each period for which a statement of income is presented?  
[SFAS 95, par. 3 (AC C25.101)]

YES NO N/A

B. Are cash receipts and cash payments from operating activities shown separately on the statement of cash flows?  
[SFAS 95, pars. 27-28 (AC C25.125-.126)]

YES NO N/A

1. Are cash receipts and payments from purchases and sales of securities and other assets acquired for resale and carried at market value in a trading account, classified as operating cash flows?  
[SFAS 102, par. 8 (AC C25.122A)]

YES NO N/A

2. Are cash receipts and payments resulting from acquisitions and sales of loans (if those loans are acquired specifically for resale and are carried at market value or the lower of cost or market) classified as operating cash flows?  
[SFAS 102, par. 9 (AC C25.122B)]

YES NO N/A
C. Are cash receipts and cash payments for the following transactions classified as cash flows from operating activities?
[SFAS 95, pars. 22-23 (AC C25.120-.121)]

1. Cash receipts from sales of goods or services, such as premiums collected. ___ ___ ___
2. Cash receipts from interest and dividends. ___ ___ ___
3. All other cash receipts that do not stem from transactions defined as investing or financing activities. ___ ___ ___
4. Cash payments to suppliers and employees, such as losses and loss adjustment expenses paid. ___ ___ ___
5. Cash payments to governments for taxes, duties, fines, and other fees or penalties. ___ ___ ___
6. Cash payments to lenders and other creditors for interest. ___ ___ ___
7. All other cash payments that do not stem from transactions defined as investing or financing activities. ___ ___ ___

D. Are cash receipts and cash payments from investing activities shown separately on statement of cash flows?
[SFAS 95, par. 31 (AC C25.129)]

E. Are cash receipts and cash payments for the following transactions classified as cash flows from investing activities?
[SFAS 95, pars. 16-17 (AC C25.114-.115)]

1. Receipts from collections or sales of loans. ___ ___ ___
2. Receipts from sales of property or investments. ___ ___ ___
3. Loans to other entities. ___ ___ ___
4. Payments to acquire property or investment. ___ ___ ___

F. Are cash receipts and cash payments from financing activities shown separately on the statement of cash flows?
[SFAS 95, par. 31 (AC C25.129)]

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G. Are cash receipts and cash payments for the following transactions classified as cash flows from financing activities?

[SFAS 95, pars. 19-20 (AC C25.117-.118)]

1. Proceeds from issuing debt or capital stock.  

2. Repayment of amounts borrowed.  

3. Dividend payments to shareholders.  

4. Acquisition of treasury stock.  

H. If applicable, is the effect of exchange rate changes on cash balances held in foreign currencies shown separately on statement of cash flows?

[SFAS 95, par. 25 (AC C25.123)]

I. Does the statement of cash flows explain the effect of cash flows by showing the change in cash and cash equivalents?

[SFAS 95, par. 7 (AC C25.105)]

J. Is the policy for defining cash equivalents disclosed?

[SFAS 95, par. 10 (AC C25.108)]

K. Is a reconciliation of net income to net cash flow from operating activities presented either within the statement of cash flows or in a separate schedule?

[SFAS 95, par. 29-30 (AC C25.127-.128)]

L. Are noncash investing and financing activities, such as converting debt to equity, summarized in a separate schedule?

[SFAS 95, par. 32 (AC C25.134)]

M. If the indirect method is used, are the amounts of interest paid (net of amounts capitalized) and income taxes paid during the period(s) disclosed?

[SFAS 95, par. 29 (AC C25.127)]
Auditors' Reports Checklist

This checklist has been developed by the staff of the Technical Information Division of the AICPA as a nonauthoritative practice aid.

Explanation of References:

AR = Reference to section number in AICPA Professional Standards (vol. 2) of SSARS cited
AU = Reference to section number in AICPA Professional Standards (vol. 1) of SAS cited
IAG = Industry Audit Guide, Audits of Stock Life Insurance Companies
SAS = Statement on Auditing Standards
SOP = Statement of Position - AICPA Auditing Standards Division
SSARS = Statement on Standards for Accounting and Review Services

Checklist Questionnaire

YES NO N/A

1. Does the auditor's report include:

   a. Addressee?
      [SAS 58, par. 9 (AU 508.09)]
      _____ _____ _____

   b. Date (or dual dates) of the report?
      [SAS 1, sec. 530 (AU 530); SAS 58, par. 46 (AU 508.46); SAS 26, pars. 15-17 (AU 504.15-.17)]
      _____ _____ _____

   c. A title that includes the word "independent"?
      [SAS 58, par. 8 (AU 508.08)]
      _____ _____ _____

2. If the auditor is not independent, was the appropriate disclaimer expressed:

   a. For a public entity?
      [SAS 26, pars. 8-10 (AU 504.08-.10)]
      _____ _____ _____

   b. For a nonpublic entity?
      [SSARS No. 1, pars. 22 and 38 (AR 100.22 and .38)]
      _____ _____ _____

3. Is the reporting language appropriate for:
   [SAS 58, par. 8 (AU 508.08)]

   a. Financial statements of a single year or period?
      _____ _____ _____
b. Comparative financial statements? ___ ___ ___

4. Does the auditor's report include appropriate language for the following?

a. The auditor's opinion is based in part on the report of another auditor. ___ ___ ___
   [SAS 58, pars. 12-13 (AU 508.12-.13)]

b. Departure from a promulgated accounting principle which could result in a misleading financial statement. ___ ___ ___
   [SAS 58, pars. 14-15 (AU 508.14-.15)]

c. The financial statements were affected by uncertainties concerning future events, the outcome of which is not susceptible to reasonable estimation. ___ ___ ___
   [SAS 58, pars. 16-33 (AU 508.16-.33)]

d. The auditor concludes substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time remains and that conclusion is expressed through the use of the phrase "substantial doubt about its (the Company's) ability to continue as a going concern". ___ ___ ___
   [SAS 64, par. 1 (AU 341.12)]

e. There was a material change between periods in accounting principles or in the method of their application. ___ ___ ___
   [SAS 58, pars. 34-36 (AU 508.34-.36)]

f. Opinion on prior-period financial statements different from the opinion previously expressed. ___ ___ ___
   [SAS 58, pars. 77-78 (AU 508.77-.78)]

g. Predecessor auditor's report reissued. ___ ___ ___
   [SAS 58, pars. 80-82 (AU 508.80-.82)]

h. Selected quarterly financial data required by the SEC was omitted or was not reviewed. ___ ___ ___
   [SAS 36, par. 29 (AU 722.29)]

i. Required supplemental information:
   [SAS 52 (AU 551.15)] ___ ___ ___
   (1) Was omitted.
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<td>(2)</td>
<td>Presentation of information departs materially from FASB guidelines.</td>
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<td>(3)</td>
<td>The auditor is unable to complete prescribed procedures.</td>
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<td>(4)</td>
<td>The auditor has substantial doubt the information conforms to FASB guidelines.</td>
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<td>j.</td>
<td>Other information in the document containing the audited financial statements is materially inconsistent with information appearing in the financial statements.</td>
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<td>k.</td>
<td>A matter regarding the financial statement that should be emphasized.</td>
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<td>l.</td>
<td>Report on one basic financial statement and there are no scope limitations.</td>
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<td>m.</td>
<td>Reports on comparative financial statements.</td>
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<td>n.</td>
<td>For comparative financial statements, there is an unqualified opinion on one of the financial statements and a qualified or adverse opinion, a disclaimer, or an explanatory paragraph on one or more financial statements for one or more periods.</td>
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<td>o.</td>
<td>Comparative financial statements with an opinion different from the opinion previously expressed.</td>
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<td>p.</td>
<td>Comparative financial statements when predecessor auditor's report not presented.</td>
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<td>q.</td>
<td>Audited and unaudited financial statements in comparative form.</td>
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r. Report on comparative statements of income, retained earnings, and cash flows without presentation of comparative balance sheets for the prior periods.
[SAS 58, par. 8, fn. 7 (AU 508.08, fn. 7)]

s. If the effects of variances from generally accepted accounting principles were determined to be material to one or more but not all of the financial statements, does the report take exception to only the statements so affected and include an unqualified opinion on the statements not affected?
[SAS 58, par. 76 (AU 508.76); IAG, p. 121]

t. A change in financial reporting from a regulatory basis to GAAP or vice versa?

5. If the financial statements of a prior period have been audited by a predecessor auditor whose report is not presented, has the successor auditor indicated in the introductory paragraph:
[SAS 64, par. 2 (AU 508.83)]

a. The financial statements of the prior period were audited by another auditor?

b. The date of the report?

c. The type of report issued by the predecessor auditor?

d. If the report was other than a standard report the substantive reasons therefor?

6. If the financial statements have been restated, does the introductory paragraph indicate that a predecessor auditor reported on the financial statements of the prior period before restatement?
[SAS 64, par. 2 (AU 508.83)]

7. If the successor auditor applies sufficient procedures to satisfy himself as to the appropriateness of any restatement adjustments made by the predecessor auditor, does the report comply with SAS 64, paragraph 2?
[SAS 64, par. 2 (AU 508.83)]
8. If, following a pooling-of-interest transaction, an auditor is engaged to report on restated financial statements for one or more prior years when other auditors audited one or more of the entities included in such financial statements, does the report include explanatory language in accordance with SAS No. 64, paragraph 3?
[SAS 64, par. 3 (AU 543.16)]

9. Is a qualified opinion or disclaimer of opinion expressed if:

a. There is a lack of sufficient competent evidential matter or there are restrictions on the scope of the audit?
[SAS 31, par. 22 (AU 326.23); SAS 58, pars. 40-48 (AU 508.40-.48)]

b. The financial statements are prepared in conformity with regulatory practices, and when the effects of the variances from generally accepted accounting principles have not been determined, has a disclaimer of opinion been issued?
[SAS 62, pars. 22-30 (AU 623.22-.30); IAG, p. 120]

10. Is a qualified opinion or adverse opinion expressed if the following circumstances are present?

a. An uncertainty is not adequately disclosed in the financial statements.
[SAS 58, par. 20 (AU 508.20)]

b. The accounting principles used cause the financial statements to be materially misstated.
[SAS 58, par. 21 (AU 508.21)]

c. The financial statements are prepared in conformity with regulatory practices, and when the effects of the variances from generally accepted accounting principles are so material that, in the auditor's judgment, a qualified opinion is not justified.
[SAS 62, pars. 22-30 (AU 623.22-.30); IAG, p. 119]
d. There are unreasonable accounting estimates that cause the financial statements to be misstated. 
[SAS 58, par. 22 (AU 508.22)]

---

e. The financial statements contain a material departure from GAAP, inadequate disclosure, or an accounting change. 
[SAS 54, par. 18 (AU 317.18); SAS 32, par. 3 (AU 431.03); SAS 59, par. 12 (AU 341.12)]

---

f. Management has represented that a material related party transaction was consummated on terms equivalent to those that prevail in arm's-length transactions and the auditor believes that this representation is unsubstantiated by management.

---

g. Client's voluntarily including supplementary information which has not been audited and the auditor has not included a disclaimer on the information in an explanatory paragraph at the end of his report. 
[SAS 52, par. 3 (AU 558.03)]

---

h. The financial statements are materially affected by an irregularity. 
[SAS 53, par. 26 (AU 316.26)]

---

i. An illegal act that has a material effect on the financial statements was not properly accounted for or disclosed. 
[SAS 54, par. 18 (AU 317.18)]

---

11. Is an adverse opinion expressed if the financial statements do not present fairly, in the auditor's judgment, the financial position or the results of operations and cash flows in conformity with GAAP? 
[SAS 58, pars. 67-69 (AU 508.67-.69)]

---

12. Is a disclaimer of opinion expressed on the financial statements when the auditor has not performed an audit sufficient in scope to enable him to form an opinion? 
[SAS 58, par. 70 (AU 508.70)]
a. Have any reservations regarding the fair presentation in conformity with generally accepted accounting principles been disclosed?  
[SAS 58, par. 71 (AU 508.71)]  

13. If a qualified opinion, adverse opinion, or disclaimer of opinion is expressed:

a. Are all the substantive reasons for the opinion or disclaimer disclosed?  
[SAS 58, pars. 39, 40, 51, 68 and 71 (AU 508.39, .40, .51, .68 and .71)]  

b. Is the reporting language clear and appropriate for the:

(1) Qualified opinion?  
[SAS 58, pars. 38-66 (AU 508.38-.66)]  

(2) Adverse opinion?  
[SAS 58, pars. 67-69 (AU 508.67-.69)]  

(3) Disclaimer of opinion?  
[SAS 58, pars. 70-72 (AU 508.70-.72)]  

14. Does the auditor’s report include modification, if applicable, for the following?

a. Conditions that precluded application of necessary auditing procedures to long-term investments.  
[SAS 58, par. 42 (AU 508.42)]  

b. Regulated companies.  
[SAS 1, sec. 544.02-.04 (AU 544.02-.04); SAS 62, pars. 2-8 (AU 623.02-.08)]  

c. Inadequate disclosure.  
[SAS 58, pars. 55-58 (AU 508.55-.58)]  

d. Client representations about related-party transactions.  
[SAS 45, par. 2 (AU 334.12)]  

e. Client’s refusal to provide written representations.  
[SAS 19, par. 11 (AU 333.11)]  

f. Limitations on scope of lawyer’s response.  
[SAS 12, pars. 12-14 (AU 337.12-.14)]
g. Unresolved matters involving specialists. ___ ___ ___  
[SAS 11, par. 9 (AU 336.09)]

h. Scope limitation concerning errors or irregularities. ___ ___ ___  
[SAS 53, par. 27 (AU 316.27)]

i. Illegal acts by clients. ___ ___ ___  
[SAS 54 (AU 317)]

j. Segment information. ___ ___ ___  
[SAS 21 (AU 435)]

k. Substantial doubt about the Company's continued existence. ___ ___ ___  
[SAS 59, pars. 12-16 (AU 341.12-.16)]

l. Material misstatement of the financial statements. ___ ___ ___  
[SAS 47, par. 31 (AU 312.31)]

m. Financial statements issued before the effective date of a SFAS when disclosure is not made of the effect of a restatement which will be required in the future as a result of the SFAS (for example, evaluate the prospective effects of SFAS 106). ___ ___ ___  
[Interpretation 3 of SAS 1, section 410 (AU 9410.13-.15)]

n. Client's voluntarily including supplementary information which was not audited. ___ ___ ___  
[SAS 52, par. 3 (AU 558.03)]

o. If the financial statements are prepared on a statutory basis, are they suitably titled (e.g., statement of income—statutory basis)? ___ ___ ___  
[SAS 62, par. 7 (AU 623.07)]

(1) If not suitably titled, are the auditor's reservations disclosed in an explanatory paragraph and a qualified report issued? ___ ___ ___

15. Has a piecemeal opinion been avoided? ___ ___ ___  
[SAS 58, par. 73 (AU 508.73); SAS 62, par. 12 (AU 623.12)]

16. For special reports, have the provisions of SAS 35 and SAS 62 been complied with for the following?
a. Statements prepared in accordance with a comprehensive basis of accounting other than generally accepted accounting principles.  
[SAS 62, pars. 2-8 (AU 623.02-.08)]  

b. Specified elements, accounts or items of a financial statement.  
[SAS 62, pars. 11-14 (AU 623.11-.14); SAS 35 (AU 622)]  

c. Compliance with aspects of contractual agreements or regulatory requirements relating to audited financial statements.  
[SAS 62, pars. 19-21 (AU 623.19-.21)]  

d. Financial information that requires a prescribed form of auditor's report.  
[SAS 62, pars. 22-26 (AU 623.22-.26)]  

17. If information is to accompany the basic financial statements and auditor's report in an auditor-submitted document:  

a. Is there a clear distinction between the client's representations and the auditor's representations?  
[SAS 29, par. 20 (AU 551.20)]  

b. Does the auditor's report on the accompanying information:  
[SAS 29, par. 6 (AU 551.06)]  

(1) State that the audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole?  

(2) Specifically identify the accompanying information?  

(3) State that the accompanying information is presented for purposes of additional analysis and is not part of the basic financial statements?  

(4) State whether the additional information was subjected to the auditing procedures applied in auditing the basic financial statements and is the appropriate expression or disclaimer of opinion included?
18. If an auditor-submitted document with accompanying information coexists with a document that includes just the basic financial statements and auditor's report:

a. Do the basic financial statements in all coexisting documents consistently include all the information necessary for a fair presentation in conformity with generally accepted accounting principles?  
[SAS 29, par. 21 (AU 551.21)]  

b. Are any additional comments or explanations by the auditor consistent with the description of the scope of the audit in the auditor's standard (or modified) report?  
[SAS 29, par. 20 (AU 551.20)]

19. If the document contains interim financial information, was the auditor's report expanded if required?  
[SAS 36, pars. 24-30 (AU 722.24-.30)]

20. If supplementary information required by the FASB is presented outside the basic financial statements in an auditor-submitted document, was an opinion disclaimed on such information unless it was audited?  
[SAS 29, par. 7 (AU 551.07); SAS 27, pars. 8 and 11 (AU 558.08 and .11)]

21. If the Company is subject to FASB requirements to include certain supplementary information in documents containing audited financial statements, was the auditor's report appropriately modified if:  
[SAS 52, par. 2 (AU 558.08)]

a. Required supplementary information is omitted?  

b. Measurement or presentation of the supplementary information departs materially from guidelines prescribed by the FASB?  

C. The auditor is unable to complete the procedures prescribed by SAS 52?
22. If a report on internal accounting control is to be issued to the audit committee or board of directors as required by SAS 60 (AU 325) (refer to NAIC Model Rule Section 11 for more detail), is the appropriate form used for:

a. Expression of an opinion on the Company's system of internal accounting control in effect as of a specified date or during a specific period of time?
   [SAS 30, pars. 37-46 (AU 642.37-.46)]

b. Communication to the audit committee of internal control structure related matters noted in an audit or other agreed upon matters?
   [SAS 60, pars. 12-19 (AU 325.12-.19)]

c. Report on all or part of the Company's system of internal accounting controls for restricted use of management or specified regulatory agencies, based on the regulatory agencies' pre-established criteria?
   [SAS 30, pars. 54-59 (AU 642.54-.59)]

d. Other special purpose reports on all or part of the Company's system for restricted use of management, specified regulatory agencies, or other specified third parties?
   [SAS 30, pars. 60-61 (AU 642.60-.61); SAS 44, pars. 35, 41 and 46 (AU 324.35, .41 and .46)]

23. If reporting in a client-prepared document on condensed financial statements (either for an annual or an interim period) derived from audited financial statements of a public entity that is required to file, at least annually, complete audited financial statements with a regulatory agency, does the auditor's report indicate:
   [SAS 42, par. 5 (AU 552.05)]

a. The auditor has audited and expressed an opinion on the complete financial statements?

b. The date of the report on the complete financial statements?

c. The type of opinion expressed?
d. Whether, in the auditor's opinion, the information set forth in the condensed financial statements is fairly stated in all material respects in relation to the complete financial statements from which it has been derived?  

24. If a statement that names the auditor and also states that condensed financial statements were derived from audited financial statements is made in a client-prepared document that does not include audited financial statements, and the client is not a public entity that is required to file complete audited financial statements with a regulatory agency, at least annually, does the auditor's report express a qualified or adverse opinion on the condensed financial statements because of inadequate disclosure? 

[SAS 58, par. 55 (AU 508.55); SAS 42, par. 7, fn. 6 (AU 552.07, fn. 6)]

25. If reporting on selected financial data included in a client-prepared document that contains audited financial statements (or, with respect to a public entity, that incorporates such statements by reference to information filed with a regulatory agency) and that is derived from audited financial statements, does the auditor's report indicate the following? 

[SAS 42, par. 9 (AU 552.09)]

a. That the auditor has examined and expressed an opinion on the complete financial statements.  

b. The type of opinion expressed.  

c. The specific data on which the auditor is reporting.  

d. Whether, in the auditor's opinion, the information in the selected financial data is fairly stated in all material respects in relation to the complete financial statements from which it has been derived.
26. If the selected financial data for any of the years presented are derived from financial statements audited by another independent auditor, does the auditor's report on the selected financial data state that fact and express a disclaimer of opinion on that data? ___ ___ ___ [SAS 42, par. 9 (AU 552.09)]
Supplemental Checklist for Property and Liability Insurance Companies That Are SEC Registrants

This supplemental checklist for property and liability insurance companies contains additional disclosures required in financial statements of property and liability insurance companies that are SEC registrants. References in this supplement are from SEC rules and regulations, because there is no specific counterpart under GAAP. This checklist covers SEC disclosures required by Article 7 of Regulation S-X which relates to financial statements filed for insurance companies. Many of these disclosures are routinely made by property and liability insurance companies even though they are not covered under the Securities Exchange Act of 1934.

Except as permitted by the SEC, the disclosures, if applicable, should appear on the face of the financial statements or in the notes thereto.

See Financial Statements and Notes Checklist for explanation of references.

<table>
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<th>Balance Sheet</th>
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A. Investments Other Than Investments in Related Parties (Reg. S-X, Rule 7-03-1 and SAB Topic No. 6)

1. Do the following captions appear separately on the balance sheet?

   a. Fixed maturities including bonds, notes, marketable certificates of deposits with maturities beyond one year and redeemable preferred stocks.

   b. Equity securities, including common stocks and nonredeemable preferred stocks.

   c. Mortgage loans on real estate.

   d. Investment real estate excluding real estate acquired in settling title claims, mortgage guaranty and insurance claims (which should be included in "Other Assets").
(1) Is the amount of accumulated depreciation and amortization deducted disclosed in the balance sheet or in the notes to financial statements? YES NO N/A

e. Policy loans. YES NO N/A

f. Other long-term investments. YES NO N/A

(1) Do the notes state the amount of any class of investment exceeding 10% of stockholders' equity? YES NO N/A

g. Short-term investments, including investments maturing in one year—commercial paper, marketable certificates of deposit, savings accounts, time deposits, cash accounts or cash equivalents earning interest. YES NO N/A

(1) Do the notes disclose any amounts subject to withdrawal or usage restrictions? YES NO N/A

h. Total Investments. YES NO N/A

2. Does the balance sheet include, parenthetically or otherwise:

a. The basis of determining the investment amounts shown in the balance sheet? YES NO N/A

b. The aggregate cost or aggregate carrying value at the balance sheet date of fixed maturities and equity securities? YES NO N/A

3. Has consideration been given to discussion of "Valuation Securities" in Section 403.03 of the SEC Codification of Financial Reporting Practices? YES NO N/A

4. Has consideration been given to disclosure of material changes in market value of investments between balance sheet date and report date? YES NO N/A

5. Do the notes state the name of any person in which the total amount invested (aggregate indebtedness, stocks issued and real estate purchased) in the person and its affiliates, exceeds 10% of total stockholders' equity? YES NO N/A
a. Is the amount included in each subcaption disclosed? (No disclosure needs to be made of investments in bonds and notes of the United States Government or its agencies that exceed 10% of stockholders' equity.)

6. For investments in fixed maturities, mortgage loans on real estate, investment real estate and other long-term investments, do the notes disclose the amount of non-income-producing investments for the twelve months preceding the balance sheet date?

B. Cash (Reg. S-X, Rule 7-03-2)

1. Is cash on hand or on deposit restricted as to withdrawal or usage disclosed separately on the balance sheet?

a. Are the provisions of any restrictions (including legally restricted deposits held as compensating balances, contracts entered into with others or the companies' intentions about particular deposits) described in the notes?

b. Are non-legally restricted compensating balance arrangements disclosed?

c. Do the notes disclose compensating balances maintained under an agreement to assure future credit availability?

C. Securities and Indebtedness of Related Parties (Reg. S-X, Rule 7-03-3)

1. Are investments in related parties disclosed?

2. Is indebtedness from related parties disclosed?

D. Accrued Investment Income (Reg. S-X, Rule 7-03-4)

1. Is the amount of accrued investment income reported separately?

E. Accounts and Notes Receivable (Reg. S-X, Rule 7-03-5)

1. Are the amounts receivable from agents and insureds included?
2. Is the amount of uncollected premiums included?  

3. Are other receivables included?  
   a. Is there separate disclosure in the notes or in the balance sheet of any "other receivable" in excess of 5% of total assets?  

4. Is the amount of the allowance for doubtful accounts disclosed separately, in the balance sheet or in a note?  

F. Reinsurance Recoverable on Paid Losses (Reg. S-X, Rule 7-03-6)  
   1. Are the amounts disclosed?  

G. Deferred Policy Acquisition Costs (Reg. S-X, Rule 7-03-7)  
   1. Are the amounts disclosed?  

H. Property and Equipment (Reg. S-X, Rule 7-03-8)  
   1. Is the basis of determining the amounts disclosed?  
   2. Do the balance sheet or the notes disclose the amount of accumulated depreciation and amortization of property and equipment?  

I. Title Plant (Reg. S-X, Rule 7-03-9)  
   1. Is the amount disclosed?  

J. Other Assets (Reg. S-X, Rule 7-03-10)  
   1. Is there separate disclosure on the balance sheet or in the notes of the amount of any "other asset" in excess of 5% of total assets?  

K. Assets Held in Separate Accounts (Reg. S-X, Rule 7-03-11)  
   1. Does the caption include aggregate amount of assets used to fund liabilities related to variable annuities, pension funds and similar activities?
2. Do the notes to the financial statements describe the general nature of the activities being reported on in the separate accounts? YES NO N/A

L. Policy Liabilities and Accruals (Reg. S-X, Rule 7-03-13, SAB Nos. 62, 74 and 87 and FRR No. 20)

1. Is the amount of future policy benefits and losses, and claims and losses separately disclosed in the balance sheet? YES NO N/A

2. Is the amount of unearned premiums separately disclosed in the balance sheet? YES NO N/A

3. Are other policy claims and benefits payable separately disclosed in the balance sheet? YES NO N/A

4. Do the notes disclose the basis of assumptions (interest rates, mortality, withdrawals) for future policy benefits and claims and settlements stated at present value? YES NO N/A

5. Do the notes disclose the general nature of reinsurance transactions, including a description of significant types of reinsurance agreements executed? YES NO N/A

   a. Do the disclosures include the nature of the contingent liability in connection with insurance ceded? YES NO N/A

   b. Do the disclosures include the nature and effect of material nonrecurring reinsurance transactions? YES NO N/A

6. If the Company has not yet adopted SFAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," have the following disclosures been considered? YES NO N/A

   a. A brief description of SFAS 106, the date that adoption is required and the date that the Company plans to adopt (if earlier). YES NO N/A

   b. A discussion of the methods of adoption allowed by SFAS 106 and the method expected to be utilized by the Company, if determined. YES NO N/A
c. A discussion of the impact that adoption of SFAS 106 is expected to have on the financial statements of the Company, unless not known or reasonably estimable. In that case, a statement to that effect may be made.  

--- YES NO N/A ---

d. Disclosure of the potential impact of other significant matters that the Company believes might result from the adoption of SFAS 106 (such as technical violations of debt covenant agreements, planned or intended changes in business practices).

--- YES NO N/A ---

e. If the Company adopts a new policy or changes its existing policy of discounting certain unpaid claims liabilities relating to short-duration insurance contracts, is the appropriate disclosure made in accordance with SAB 62?

--- YES NO N/A ---

f. Are the appropriate disclosures made concerning reserves for unpaid claims and claim adjustment expenses in accordance with FRR No. 20 for the following areas?

a. Certain significant transactions during the reporting periods.

--- YES NO N/A ---

b. Changes in historical reserve amounts for the latest ten years.

--- YES NO N/A ---

c. The Company's reserving practices, including those used in estimating inflation, and any significant changes in these practices.

--- YES NO N/A ---

d. The effect, if any, of the discounting of reserves.

--- YES NO N/A ---

e. Any difference between reserves reflected in reports to state regulatory authorities and those appearing in GAAP financial statements.

--- YES NO N/A ---

g. Has the Company considered the disclosures regarding contingency on property-casualty insurance reserves for unpaid claims discussed in SAB No. 87?

--- YES NO N/A ---
M. Other Policyholders' Funds (Reg. S-X, Rule 7-03-14)

1. Does the caption include the aggregate amount of supplementary contracts without life contingencies, policyholders' dividend accumulations, undistributed earnings on participating policies, dividends to policyholders and retrospective return premiums and similar items? ___ ___ ___

2. Is there separate disclosure in the balance sheet or in the notes of any item the amount of which is in excess of 5% of total liabilities? ___ ___ ___

3. Do the notes disclose the relative significance of participating insurance as a percentage of (1) insurance in force and (2) premium income? ___ ___ ___
   a. Do the notes disclose the method by which earnings and dividends allocable to such insurance is determined? ___ ___ ___

N. Other Liabilities (Reg. S-X, Rule 7-03-15)

1. Is there separate disclosure in the balance sheet or in the notes of any item the amount of which is in excess of 5% of total liabilities? ___ ___ ___

2. Is there separate disclosure in the balance sheet or in the notes of (1) income taxes currently payable and (2) deferred income taxes? ___ ___ ___
   a. Is there separate disclosure of the amount of deferred income taxes applicable to unrealized appreciation of equity securities? ___ ___ ___

O. Notes Payable, Bonds, Mortgages and Similar Obligations, Including Capitalized Leases (Reg. S-X, Rule 7-03-16)

1. Is the amount of short-term debt separately disclosed? ___ ___ ___
   a. If the aggregate of short-term borrowings (from banks, factors and other financial institutions and commercial paper issued) exceeds 5% of total liabilities, do the notes disclose the amount and terms (in-
incluing commitment fees and the conditions under which lines may be withdrawn) of unused lines of credit for short-term financing?
(Reg. S-X, Rule 5-02-19(b))

b. Is the amount of the lines of credit that support commercial paper borrowing arrangements separately identified?
(Reg. S-X, Rule 5-01-19(b))

2. Is the amount of long-term debt including capitalized leases separately disclosed?

a. Is there disclosure of the general character of each type of debt?

b. Is the interest rate disclosed?

c. Is the maturity date or, if maturing serially, a brief indication of the serial maturities disclosed?

d. If the payment of principal or interest is contingent, is there appropriate indication of such contingency?

e. Is there a brief indication of priority?

f. If convertible, is the basis disclosed?
(Reg. S-X, Rule 5-02-22)

P. Indebtedness to Related Parties (Reg. S-X, Rules 7-03-17 and 4-08(k))

1. Are related party transactions identified and the amount stated on the face of the balance sheet, income statement or statement of cash flows?

2. If there are separate financial statements for the registrant, certain investees or subsidiaries, is there separate disclosure of the amounts in the related consolidated statements that are (1) eliminated and (2) not eliminated?

3. If any intercompany profit or losses resulting from transactions with related parties are not eliminated, are the effects disclosed?
Q. Liabilities Related to Separate Accounts (Reg. S-X, Rule 7-03-18)

1. Is the amount disclosed? ___ ___ ___

R. Commitments and Contingent Liabilities (Reg. S-X, Rule 7-03-19)

1. Have the proper disclosures been made? ___ ___ ___

S. Minority Interest in Consolidated Subsidiaries (Reg. S-X, Rule 7-03-20 and Rule 5-02-27)

1. Do the notes disclose the amounts represented by preferred stock and the applicable dividend requirements? ___ ___ ___

T. Preferred Stock Subject to Mandatory Redemption (Reg. S-X, Rule 7-03-21 and Rule 5-02-28)

1. Is the title of each issue, the carrying amount and redemption amount stated on the balance sheet? ___ ___ ___

2. Is the dollar amount of any shares subscribed but unissued shown together with the deduction of subscriptions receivable? ___ ___ ___

3. If the carrying value is different from the redemption amount, is there a description of the accounting treatment for such difference? ___ ___ ___

4. Is there disclosure, for each issue, of the number of shares authorized, issued and outstanding? ___ ___ ___

U. Nonredeemable Preferred Stock (Reg. S-X, Rule 7-03-22 and Rule 5-02-29)

1. Is the title of each issue and the carrying amount disclosed on the balance sheet or in the notes? ___ ___ ___

2. Is the dollar amount of any shares subscribed but unissued shown together with the deduction of subscriptions receivable? ___ ___ ___

3. Is there disclosure, for each issue, of the number of shares authorized, issued and outstanding? ___ ___ ___
4. Is there disclosure in a note or in a separate statement of the changes in each class of preferred stock for which an income statement is required to be filed?  YES NO N/A

V. Common Stock (Reg. S-X, Rule 7-03-23 and Rule 5-02-30)

1. Does the face of the balance sheet disclose the number of shares issued and outstanding?  YES NO N/A

2. If convertible, is that fact indicated on the face of the balance sheet?  YES NO N/A

3. Is there disclosure, for each class of common stock, of the title of each issue, the number of shares authorized and the basis of conversion?  YES NO N/A

4. Is the dollar amount of any shares subscribed but unissued shown together with the deduction of subscriptions receivable?  YES NO N/A

5. Do the notes or a separate statement disclose the changes in each class of common stock for which an income statement is required to be filed?  YES NO N/A

W. Other Stockholders' Equity (Reg. S-X, Rule 7-03-24, Rules 5-02-31(b) and (c))

1. Are separate captions shown for:
   a. Additional paid-in capital?  YES NO N/A
   b. Other additional capital?  YES NO N/A
   c. Unrealized appreciation or depreciation of equity securities less applicable deferred income taxes?  YES NO N/A
   d. Appropriated retained earnings?  YES NO N/A
   e. Unappropriated retained earnings?  YES NO N/A

2. If there has been a quasi reorganization in the last 10 years, has the retained earnings account been dated?  YES NO N/A
3. Do the notes disclose, for each life insurance and property and liability legal entity, the amount of statutory stockholders' equity as of the date of each balance sheet presented?  

4. Is there disclosure of the amount of statutory net income or loss for each period for which an income statement is presented?

Income Statement

A. Premiums (Reg. S-X, Rule 7-04-1)

1. Do the amounts included in this caption represent premiums earned?

B. Net Investment Income (Reg. S-X, Rule 7-04-2)

1. Do the notes disclose the amount of investment income for each category of investment listed in the balance sheet (caption A) above that exceeds 5% of total investment income?

2. Do the notes disclose total investment income?

3. Do the notes disclose applicable investment expenses?

4. Do the notes disclose net investment income?

C. Other Income (Reg. S-X, Rule 7-04-3)

1. Are items in excess of 5% of total revenue separately disclosed?

D. Benefits, Claims, Losses and Settlement Expenses (Reg. S-X, Rule 7-04-4)

1. Have the amounts been disclosed?

E. Policyholders' Share of Earnings on Participating Policies, Dividends and Similar Items [Reg. S-X, Rules 7.04-5 and 7-03-14(b)]

1. Have the amounts been disclosed?

F. Underwriting, Acquisition and Insurance Expenses (Reg. S-X, Rule 7-04-6)

1. Do the statements or notes disclose:
a. The amount of deferred policy acquisition cost amortized to income for each period?  

b. The amount of other operating expenses with separate disclosure of any material amounts?

G. Income Tax Expense [Reg. S-X, Rules 7-04-8 and 4-08(h)]

1. Does the income statement or notes disclose:
   a. The domestic component of income (loss) before income tax expense (benefit)?
   b. The foreign component of income (loss) before income tax expense (benefit)?
   c. Taxes currently payable?
   d. The net tax effects of timing differences?

2. Is there a reconciliation between the amount of reported total income tax expense (benefit) and the amount of tax computed at the applicable statutory federal income tax rate?

H. Minority Interest in Income of Consolidated Subsidiaries (Reg. S-X, Rule 7-04-9)

1. Were the amounts disclosed?

I. Equity in Earnings of Unconsolidated Subsidiaries and 50 Percent or Less Owned Persons (Reg. S-X, Rule 7-04-10)

1. Was the amount stated net of any applicable tax provision?
2. Were gains or losses on investments excluded?
3. Was the amount of dividends received disclosed?

J. Discontinued Operations (Reg. S-X, Rule 7-04-13)

1. Is any amount separately reported?

1. Is any amount separately reported?                   YES NO N/A

L. Cumulative Effect of Changes in Accounting Principles (Reg. S-X, Rule 7-04-16)

1. Is any amount separately reported?                   YES NO N/A

M. Earnings Per Share Data (Reg. S-X, Rule 7-04-18)

1. Have applicable amounts been reported?                YES NO N/A

N. Schedules (Reg. S-X, Rule 7-05)

1. Was Schedule Number I—Summary of Investments Other Than Investments in Related Parties (refers to Rule 7-05(c) and Rule 12-15) filed for the most recent audited balance sheet?                           YES NO N/A

2. Was Schedule Number II—Amounts Receivable From Related Parties, and Underwriters, Promoters, and Employees Other Than Related Parties (refers to Rule 7-05(c) and Rule 12-03) filed for each period for which an audited income statement is required?                        YES NO N/A

3. Was Schedule III—Condensed Financial Information of Registrant (refers to Rule 7-05(c) and Rule 12-04) filed for the periods specified in the schedule?                                  YES NO N/A

4. Was Schedule IV—Indebtedness of and to Related Parties Not Current (refers to Rule 7-05(c) and Rule 12-05) filed for each period for which an audited income statement is required?                     YES NO N/A

5. Was Schedule V—Supplementary Insurance Information (refers to Rule 7-05(c) and Rule 12-16) presented for each required balance sheet?                                                                                  YES NO N/A

6. Was Schedule VI—Reinsurance (refers to Rule 7-05(c) and Rule 12-17) filed for each period for which an audited income statement is required?                          YES NO N/A
7. Was Schedule VII—Guarantees of Securities of Other Issuers (refers to Rule 7-05(c) and Rule 12-08) filed for each period for which an audited income statement is required?  

8. Was Schedule VIII—Valuation and Qualifying Accounts (refers to Rule 7-05(c) and Rule 12-09) filed for each period for which an audited income statement is required?  

9. Was Schedule IX—Short-term Borrowings (refers to Rule 7-05(c) and Rule 12-10) filed for each period for which an audited income statement is required?  

10. Was Schedule X—Supplemental Information Concerning Property Casualty Insurance Operations (refers to Rule 7-05(c) and Rule 12-18) filed for the periods specified in the schedule?
Illustrative Financial Statements
ILLUSTRATIVE FINANCIAL STATEMENTS

The following report and set of financial statements illustrate one form of currently acceptable practice and, as indicated, do not include all disclosures required under generally accepted accounting principles. Other forms of financial statements are acceptable. More or less detail should appear either in the financial statement or in the notes, depending on the circumstances.
ILLUSTRATIVE INDEPENDENT AUDITOR’S REPORT

To the Board of Directors and Stockholders
The Property and Liability Insurance Company
Anytowne, U.S.A.

We have audited the accompanying balance sheets of The Property and Liability Insurance Company and Subsidiaries as of December 31, 199X and 199Y, and the related statements of income, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Property and Liability Insurance Company and Subsidiaries at December 31, 199X and 199Y, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.

[Signature]

Office Town, U.S.A.
January 15, 199Z
The Property and Liability Insurance Company and Subsidiaries
Illustrative Consolidated Balance Sheet
December 31, 19X2 and 19X1
(Dollars in thousands)

<table>
<thead>
<tr>
<th>ASSETS</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investments (notes 1 and 2):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed maturities, principally at amortized cost</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(related market value, 19X2—$1,223,339; 19X1—$1,216,485)</td>
<td>$1,077,735</td>
<td>$1,023,098</td>
</tr>
<tr>
<td>Equity securities, at market (related cost, 19X2—$81,834; 19X1—$93,937)</td>
<td>90,544</td>
<td>102,771</td>
</tr>
<tr>
<td>Mortgage loans on real estate (less allowance for credit losses, 19X2—$2,300; 19X1—$2,070)</td>
<td>472,509</td>
<td>398,426</td>
</tr>
<tr>
<td>Real estate, net of accumulated depreciation (19X2—$12,921; 19X1—$12,774) and less allowance for impairment of value (19X2—$1,173; 19X1—$1,150)</td>
<td>31,905</td>
<td>30,028</td>
</tr>
<tr>
<td>Short-term investments, at cost which approximates market value</td>
<td>130,070</td>
<td>109,105</td>
</tr>
<tr>
<td>Total investments</td>
<td>1,802,763</td>
<td>1,663,428</td>
</tr>
<tr>
<td>Cash</td>
<td>31,564</td>
<td>28,357</td>
</tr>
<tr>
<td>Accrued interest and dividends</td>
<td>31,358</td>
<td>27,568</td>
</tr>
<tr>
<td>Premiums and agents' balances</td>
<td>76,640</td>
<td>74,951</td>
</tr>
<tr>
<td>Reinsurance recoverable on paid losses</td>
<td>27,908</td>
<td>24,461</td>
</tr>
<tr>
<td>Deferred policy acquisition costs (note 1)</td>
<td>168,974</td>
<td>154,941</td>
</tr>
<tr>
<td>Property and equipment, at cost, less accumulated depreciation of $17,837 in 19X2 and $15,404 in 19X1 (note 1)</td>
<td>34,443</td>
<td>27,938</td>
</tr>
<tr>
<td>Other assets</td>
<td>128,577</td>
<td>107,378</td>
</tr>
<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td><strong>$2,302,227</strong></td>
<td><strong>$2,109,022</strong></td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.
<table>
<thead>
<tr>
<th>LIABILITIES</th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Losses and loss-adjustment expenses (note 1)</td>
<td>$1,183,343</td>
<td>$1,030,345</td>
</tr>
<tr>
<td>Unearned premiums (note 1)</td>
<td>493,833</td>
<td>482,619</td>
</tr>
<tr>
<td>Dividends to policyholders</td>
<td>3,087</td>
<td>4,042</td>
</tr>
<tr>
<td>Reinsurance funds held and balances payable</td>
<td>15,727</td>
<td>35,584</td>
</tr>
<tr>
<td>Accrued expenses</td>
<td>85,780</td>
<td>82,608</td>
</tr>
<tr>
<td>Federal income taxes payable (notes 1 and 4)</td>
<td>3,166</td>
<td>7,058</td>
</tr>
<tr>
<td>Deferred income taxes (notes 1 and 4)</td>
<td>34,084</td>
<td>35,133</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>56,144</td>
<td>43,782</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>1,875,164</td>
<td>1,721,171</td>
</tr>
</tbody>
</table>

| SHAREHOLDERS' EQUITY (note 6)   |           |            |
| Common stock ($5 par value, authorized—11,500 shares; issued—2,500 shares, including 200 shares in treasury in 19X2 and 19X1) | 12,500    | 12,500    |
| Additional paid-in capital      | 22,500     | 22,500     |
| Retained earnings (notes 5 and 6) | 390,815    | 351,521    |
| Unrealized appreciation of equity securities, less applicable deferred taxes (note2) | 5,748      | 5,830      |
| Less treasury stock, at cost    | (4,500)    | (4,500)    |
| Total shareholders' equity      | 427,063    | 387,851    |

| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | $2,302,227 | $2,109,022 |

See accompanying notes to consolidated financial statements.
**The Property and Liability Insurance Company and Subsidiaries**

**Illustrative Consolidated Statements of Income**

For the Years Ended December 31, 19X2 and 19X1

*(Dollars in thousands, except per share amounts)*

<table>
<thead>
<tr>
<th>REVENUES</th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premiums earned (notes 1 and 3)</td>
<td>$570,885</td>
<td>$524,746</td>
</tr>
<tr>
<td>Net investment income</td>
<td>146,683</td>
<td>130,070</td>
</tr>
<tr>
<td>Net realized gains on investments (notes 1 and 2)</td>
<td>84,776</td>
<td>32,272</td>
</tr>
<tr>
<td>Other</td>
<td>13,288</td>
<td>8,784</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>815,632</strong></td>
<td><strong>695,872</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>EXPENSES</th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Losses and loss-adjustment expenses (notes 1 and 3)</td>
<td>$509,568</td>
<td>$432,413</td>
</tr>
<tr>
<td>Policyholder dividends (note 1)</td>
<td>4,833</td>
<td>7,395</td>
</tr>
<tr>
<td>Policy acquisition and other underwriting expenses (note 1)</td>
<td>211,239</td>
<td>185,834</td>
</tr>
<tr>
<td>Other</td>
<td>8,347</td>
<td>2,215</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td><strong>733,987</strong></td>
<td><strong>627,857</strong></td>
</tr>
<tr>
<td>Income before income taxes</td>
<td>81,645</td>
<td>68,015</td>
</tr>
<tr>
<td>Provision (benefit) for income taxes (note 4)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current</td>
<td>26,108</td>
<td>16,291</td>
</tr>
<tr>
<td>Deferred</td>
<td>(1,007)</td>
<td>881</td>
</tr>
<tr>
<td><strong>Total income taxes</strong></td>
<td><strong>25,101</strong></td>
<td><strong>17,172</strong></td>
</tr>
</tbody>
</table>

**Net Income**

<table>
<thead>
<tr>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$ 56,544</strong></td>
<td><strong>$ 50,843</strong></td>
</tr>
</tbody>
</table>

**Per Share Data**

<table>
<thead>
<tr>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$ 24.58</strong></td>
<td><strong>$ 21.18</strong></td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.
## The Property and Liability Insurance Company and Subsidiaries
Illustative Consolidated Statements of Changes in Stockholders' Equity
For the Years Ended December 31, 19X2 and 19X1
(Dollars in thousands)

<table>
<thead>
<tr>
<th>Shares</th>
<th>Amount</th>
<th>Additional Paid-in Capital</th>
<th>Unrealized Appreciation of Investments</th>
<th>Retained Earnings</th>
<th>Treasury Stock</th>
<th>Total Shareholders' Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance at January 1, 19X1</td>
<td>2,500</td>
<td>$12,500</td>
<td>$22,500</td>
<td>$3,942</td>
<td>$315,678</td>
<td>$354,620</td>
</tr>
<tr>
<td>19X1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net income</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>50,843</td>
</tr>
<tr>
<td>Dividends ($6.00 per share)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(15,000)</td>
</tr>
<tr>
<td>Increase in unrealized appreciation of investments</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,888</td>
</tr>
<tr>
<td>Purchase of 200 shares of treasury stock</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$(4,500)</td>
</tr>
<tr>
<td>Balance at December 31, 19X1</td>
<td>2,500</td>
<td>$12,500</td>
<td>$22,500</td>
<td>$5,830</td>
<td>$351,521</td>
<td>$387,851</td>
</tr>
<tr>
<td>19X2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net income</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$ 56,544</td>
</tr>
<tr>
<td>Dividends ($7.50 per share)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(17,250)</td>
</tr>
<tr>
<td>Decrease in unrealized appreciation of investments</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$(82)</td>
</tr>
<tr>
<td>Balance at December 31, 19X2</td>
<td>2,500</td>
<td>$12,500</td>
<td>$22,500</td>
<td>$5,748</td>
<td>$390,815</td>
<td>$427,063</td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.
### The Property and Liability Insurance Company and Subsidiaries
#### Illustrative Consolidated Statements of Cash Flow
For the Years Ended December 31, 19X2 and 19X1
*(Dollars in thousands)*

<table>
<thead>
<tr>
<th></th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cash flows from operating activities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premiums collected</td>
<td>$ 580,410</td>
<td>$ 536,532</td>
</tr>
<tr>
<td>Losses and loss adjustment expenses paid</td>
<td>(356,570)</td>
<td>(352,411)</td>
</tr>
<tr>
<td>Underwriting expenses paid</td>
<td>(208,067)</td>
<td>(184,006)</td>
</tr>
<tr>
<td>Investment income received</td>
<td>142,893</td>
<td>126,860</td>
</tr>
<tr>
<td>Income taxes paid</td>
<td>(30,000)</td>
<td>(21,300)</td>
</tr>
<tr>
<td>Miscellaneous receipts (payments)</td>
<td>(45,673)</td>
<td>26,266</td>
</tr>
<tr>
<td><strong>Net cash provided by operating activities</strong></td>
<td>82,993</td>
<td>131,941</td>
</tr>
</tbody>
</table>

| **Cash flows from investing activities:** |            |            |
| Proceeds from sales of investments | 585,674    | 341,906    |
| Purchase of investments           | (641,210)  | (451,627)  |
| Purchase of property and equipment | (7,000)    | (2,356)    |
| **Net cash used in investing activities** | (62,536)   | (112,077)  |

| **Cash flows from financing activities:** |            |            |
| Payment of dividends              | (17,250)   | (15,000)   |
| Purchase of treasury shares       | —          | (4,500)    |
| **Net cash used in financing activities** | (17,250)   | (19,500)   |

| **Net increase (decrease) in cash** | 3,207      | 364        |
| **Cash at beginning of year**      | 28,357     | 27,993     |
| **Cash at end of year**            | $ 31,564   | $ 28,357   |
Reconciliation of net income to net cash provided by operating activities

<table>
<thead>
<tr>
<th></th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Net income</strong></td>
<td>56,544</td>
<td>50,843</td>
</tr>
<tr>
<td><strong>Adjustments to reconcile net income</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>to net cash provided by operating activities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Depreciation</strong></td>
<td>2,580</td>
<td>2,389</td>
</tr>
<tr>
<td><strong>Gains on sales of investment</strong></td>
<td>(84,776)</td>
<td>(32,272)</td>
</tr>
<tr>
<td><strong>Increase in accrued interest and dividends</strong></td>
<td>(3,790)</td>
<td>(2,983)</td>
</tr>
<tr>
<td><strong>Increase in premium and agents’ balances</strong></td>
<td>(1,689)</td>
<td>(2,671)</td>
</tr>
<tr>
<td><strong>Increase in reinsurance recoverable</strong></td>
<td>(3,447)</td>
<td>(892)</td>
</tr>
<tr>
<td><strong>Increase in deferred policy acquisition costs</strong></td>
<td>(14,033)</td>
<td>(10,963)</td>
</tr>
<tr>
<td><strong>Increase in unpaid losses and loss adjustment expenses</strong></td>
<td>152,998</td>
<td>112,991</td>
</tr>
<tr>
<td><strong>Increase in unearned premiums</strong></td>
<td>11,214</td>
<td>9,816</td>
</tr>
<tr>
<td><strong>Decrease in dividends payable</strong></td>
<td>(955)</td>
<td>(820)</td>
</tr>
<tr>
<td><strong>Decrease in reinsurance funds held</strong></td>
<td>(19,857)</td>
<td>(18,152)</td>
</tr>
<tr>
<td><strong>Increase in accrued expenses</strong></td>
<td>3,172</td>
<td>2,915</td>
</tr>
<tr>
<td><strong>Decrease in income taxes</strong></td>
<td>(4,941)</td>
<td>(3,156)</td>
</tr>
<tr>
<td><strong>Decrease (increase) in other—net</strong></td>
<td>(10,027)</td>
<td>24,896</td>
</tr>
<tr>
<td><strong>Net cash provided by operating activities</strong></td>
<td><strong>$82,993</strong></td>
<td><strong>$131,941</strong></td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.
Illustrative Note: Summary of Significant Accounting Policies

The significant accounting policies followed by ABC Property and Liability Insurance Company and subsidiaries (the Company) are summarized as follows:

- **Principles of Consolidation:** The consolidated financial statements include the accounts, after intercompany eliminations, of the Company and its subsidiaries.

- **Basis of Presentation:** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles that differ from statutory accounting practices prescribed or permitted for insurance companies by regulatory authorities.

- **Investments:** Investments are shown on the following bases:
  - Fixed maturities (bonds, notes, and redeemable preferred stocks)—at cost, adjusted for amortization of premium or discount and other-than-temporary market value declines
  - Equity securities (common and nonredeemable preferred stocks)—at current market value
  - Mortgage loans on real estate—at unpaid balances, adjusted for amortization of premium or discount, less a provision for credit losses
  - Real estate—at cost, less allowances for depreciation and impairment of value

Realized gains and losses on sales of investments are recognized in net income on the specific identification basis. Changes in market values of equity securities, after deferred income tax effects, are reflected as unrealized appreciation or depreciation directly in shareholders' equity and, accordingly, have no effect on net income.

- **Interest Rate Futures:** The Company uses interest rate futures contracts as part of its overall interest rate risk management strategy for certain insurance products. Gains and losses on futures contracts used in asset/liability management for identified positions are deferred and amortized over the remaining lives of the hedged assets or liabilities as an adjustment to interest income or expense. When the assets or liabilities underlying the futures contracts are disposed of or eliminated, any unamortized gains or losses are recognized concurrently.

- **Recognition of Premium Revenues:** Property and liability premiums are generally recognized as revenue on a pro rata basis over the policy term.

- **Deferred Policy Acquisition Costs:** Commissions and other costs of acquiring insurance that vary with and are primarily related to the production of new and renewal business are deferred and amortized over the terms of the policies or reinsurance treaties to which they relate. Amortization in 19X2 and 19X1 was approximately $58,000,000 and $55,000,000, respectively.

- **Property and Equipment:** Property and equipment is recorded at cost and is depreciated principally under the straight-line method over the estimated useful lives of the respective assets.

- **Insurance Liabilities:** The liability for losses and loss-adjustment expenses includes an amount determined from loss reports and individual cases and an amount, based on past experience, for losses incurred but not reported. Such liabilities are necessarily based on estimates and, while management believes that the amount is adequate, the ultimate liability may be in excess of or less than the amounts provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in earnings currently. The reserve for losses and loss-adjustment expenses is reported net of receivables for salvage and subrogation of approximately $17,527,000 and $16,276,000 at December 31, 19X2 and 19X1, respectively.
• Participating Policies: Participating business represents 6 percent of total premiums in force and premium income at December 31, 19X2, and 8 percent at December 31, 19X1. The majority of participating business is composed of workers' compensation policies. The amount of dividends to be paid on these policies is determined based on the terms of the individual policies.

• Reinsurance: Reinsurance premiums, commissions, expense reimbursements, and reserves related to reinsured business are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premiums ceded to other companies have been reported as a reduction of premium income. Amounts applicable to reinsurance ceded for unearned premium reserves, and loss and loss-adjustment expense reserves have been reported as reductions of these items, and expense allowances received in connection with reinsurance ceded have been accounted for as a reduction of the related policy acquisition costs and are deferred and amortized accordingly.

• Income Taxes: Income tax provisions are based on income reported for financial statement purposes. Deferred federal income taxes arise from differences in the timing of recognizing certain income and expense items for financial statement and tax purposes. Such differences are related principally to the deferral of policy acquisition costs and the recognition of salvage and subrogation on an accrual basis.

• Income per Share of Common Stock: Income per share of common stock is based on the weighted average number of shares of common stock outstanding during each year. The effect of stock options is not material to the computation of earnings per share.

• Accounting Standards Not Yet Adopted: In 1987, the FASB issued Statement No. 96, Accounting for Income Taxes, which will have an impact on the Company's financial statements in future years. FASB Statement No. 96 establishes new principles for calculating and reporting the effects of federal income taxes in financial statements. The Board continues to study possible significant changes in the standard. The timing and method of implementing FASB Statement No. 96 by the Company has not been determined. No significant adjustment to shareholders' equity is anticipated as a result of implementing FASB Statement No. 96.

Illustrative Note: Investments

Major categories of net investment income are summarized as follows:

<table>
<thead>
<tr>
<th></th>
<th>19X2 (Dollars in thousands)</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed maturities</td>
<td>$ 93,298</td>
<td>$ 85,692</td>
</tr>
<tr>
<td>Equity securities</td>
<td>8,005</td>
<td>7,154</td>
</tr>
<tr>
<td>Mortgage loans on real estate</td>
<td>41,984</td>
<td>32,906</td>
</tr>
<tr>
<td>Real estate</td>
<td>2,537</td>
<td>2,779</td>
</tr>
<tr>
<td>Short-term investments</td>
<td>9,673</td>
<td>8,575</td>
</tr>
<tr>
<td></td>
<td>155,497</td>
<td>137,106</td>
</tr>
<tr>
<td>Investment expenses</td>
<td>8,814</td>
<td>7,036</td>
</tr>
<tr>
<td></td>
<td>$146,683</td>
<td>$130,070</td>
</tr>
</tbody>
</table>
Realized gains (losses) and unrealized appreciation on investments for the years 19X2 and 19X1 are summarized as follows:

<table>
<thead>
<tr>
<th></th>
<th>Fixed Maturities</th>
<th>Equity Securities</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Realized</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>19X2</td>
<td>($33,855)</td>
<td>$118,631</td>
<td>$84,776</td>
</tr>
<tr>
<td>19X1</td>
<td>($62,569)</td>
<td>$ 94,841</td>
<td>$32,272</td>
</tr>
<tr>
<td>Unrealized</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>19X2</td>
<td>$8,710</td>
<td>$ 2,962</td>
<td>$5,748</td>
</tr>
<tr>
<td>19X1</td>
<td>$8,834</td>
<td>$ 3,004</td>
<td>$5,830</td>
</tr>
</tbody>
</table>

At December 31, 19X2 and 19X1, gross unrealized appreciation pertaining to equity securities was approximately $106,430,000 and $118,636,000, and gross unrealized depreciation was approximately $97,720,000 and $109,802,000, respectively.

Bonds with an amortized cost of $100,000 were non-income producing for the year ended December 31, 19X2. At December 31, 19X2, bonds carried at an amortized cost of $43,684,000 were on deposit with regulatory authorities.

**Illustrative Note: Reinsurance Activity**

Substantial amounts of reinsurance are assumed, both domestic and foreign. Such reinsurance includes quota share, excess of loss, catastrophe, facultative, and other forms of reinsurance on essentially all property and casualty lines of insurance.

The Company limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring (ceding) certain levels of risks with other insurers or reinsurers, either on an automatic basis under general reinsurance contracts known as "treaties" or by negotiation on substantial individual risks. Ceded reinsurance is treated as the risk and liability of the assuming companies.

A reconciliation of direct to net premiums, on both a written and an earned basis, for 19X2 and 19X1 is as follows:

<table>
<thead>
<tr>
<th></th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Written</td>
<td>Earned</td>
</tr>
<tr>
<td>Direct</td>
<td>777,836</td>
<td>757,828</td>
</tr>
<tr>
<td>Assumed</td>
<td>306,814</td>
<td>294,577</td>
</tr>
<tr>
<td>Ceded</td>
<td>($502,551)</td>
<td>($481,520)</td>
</tr>
<tr>
<td>Net</td>
<td>$ 582,099</td>
<td>$ 570,885</td>
</tr>
</tbody>
</table>

The amounts of premiums and recoveries pertaining to catastrophe reinsurance contracts that were deducted from earned premiums and losses incurred during 19X2 were approximately $1,924,000 and $4,892,000, respectively. Such amounts for 19X1 were approximately $2,196,000 and $3,232,000, respectively.

In the event that all or any of the reinsuring companies might be unable to meet their obligations under existing reinsurance agreements, the Company would be liable for such defaulted amounts. Estimated amounts recoverable from reinsurers deducted from the reserve for losses and loss-adjustment expenses were approximately $592,622,000 and $515,172,000 for 19X2 and 19X1, respectively.
Illustrative Note: Income Taxes

The provision for federal income taxes differs from amounts currently payable due to certain items reported for financial statement purposes in periods that differ from those in which they are reported for tax purposes.

The items in the deferred tax provision are as follows:

<table>
<thead>
<tr>
<th></th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred policy acquisition costs</td>
<td>(772)</td>
<td>688</td>
</tr>
<tr>
<td>Salvage and subrogation</td>
<td>73</td>
<td>72</td>
</tr>
<tr>
<td>Other</td>
<td>(162)</td>
<td>121</td>
</tr>
<tr>
<td>Deferred tax provision</td>
<td>(1,007)</td>
<td>881</td>
</tr>
</tbody>
</table>

The liability for deferred income taxes includes the tax effect of net unrealized appreciation or depreciation on investments and other equity transactions.

The difference between taxes computed at the statutory rate and the recorded taxes is as follows:

<table>
<thead>
<tr>
<th></th>
<th>19X2</th>
<th>19X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax at statutory rate</td>
<td>$27,759</td>
<td>34.0</td>
</tr>
<tr>
<td>Tax-exempt bond interest</td>
<td>(354)</td>
<td>0.4</td>
</tr>
<tr>
<td>Dividends-received deduction</td>
<td>(125)</td>
<td>0.2</td>
</tr>
<tr>
<td>Other</td>
<td>(2,179)</td>
<td>2.7</td>
</tr>
<tr>
<td>Provision for income taxes</td>
<td>$25,101</td>
<td>30.7</td>
</tr>
</tbody>
</table>

Illustrative Note: Dividends From Subsidiaries

The funding of the cash requirements of the Company (parent company) is primarily provided by cash dividends from the Company's subsidiaries. Dividends paid by the insurance subsidiaries are restricted by regulatory requirements of the domiciliary states. Generally, the maximum dividend that may be paid without prior regulatory approval is limited to the greater of 10 percent of statutory surplus (shareholders' equity on a statutory basis) or 100 percent of net investment income for the prior year. Dividends exceeding these limitations can generally be made subject to approval by various state insurance departments. The subsidiaries paid cash dividends to the Company of $24,754,000 and $22,100,000 in 19X2 and 19X1, respectively. At December 21, 19X2, the maximum dividend that may be paid to the Company in 19X3 without regulatory approval is approximately $146,000,000.

Illustrative Note: Statutory Net Income and Shareholders' Equity

Generally accepted accounting principles differ in certain respects from the accounting practices prescribed or permitted by insurance regulatory authorities (statutory basis). Statutory net income was approximately $35,681,000 and $52,735,000 in 19X2 and 19X1, respectively, and statutory shareholders' equity was approximately $347,237,000 and $299,720,000 at December 31, 19X2 and 19X1, respectively.
Illustrative Note: Contingencies

In November 1988, California voters passed Proposition 103, requiring insurers doing business in that state to roll back property/casualty premium prices to November 1987 levels, less an additional 20 percent discount. Insurers challenged the constitutionality of Proposition 103, and in May 1989 the California Supreme Court upheld the proposition in large part. However, the Court also ruled that the rollback provision does not apply to an insurer who demonstrates through rate filings that the rate rollback would not allow a “fair and reasonable return.” The Company filed for exemption from the rate rollback for all lines affected by Proposition 103. In September 1989, the California Insurance Commissioner announced that the Company would be afforded a hearing and using different assumptions and methods than prescribed for the original filing, determined that the Company should roll back its rates and refund premiums of $19 million. The Company disagrees with the Commissioner’s methods and conclusions, and no provision for potential rate rollbacks or premium refunds is reflected in the financial results.

In October 1989, the Commissioner suspended the individual hearings and began a consolidated hearing, in which the Company is participating, intended to define the generic issue of the methods to be used to calculate potential rate rollbacks and analyze future rate filings. Until the generic issues are resolved in the Commissioner’s consolidated hearing, there will be uncertainty as to whether the Company will ultimately be required to roll back any of its rates or refund any premiums. Management believes such rate rollbacks and premium refunds, if any, would not have a material adverse effect on the Company’s financial position.
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