



STATUTORY-BASIS FINANCIAL STATEMENTS

CAMICO Mutual Insurance Company  
For the Years Ended December 31, 2009 and 2008  
With Report of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

CAMICO Mutual Insurance Company

Statutory-Basis Financial Statements

Years Ended December 31, 2009 and 2008

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## Report of Independent Auditors

The Board of Directors of  
CAMICO Mutual Insurance Company

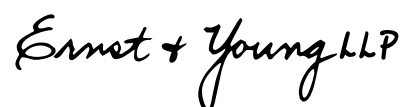
We have audited the accompanying statutory-basis statements of admitted assets, liabilities, and policyholders' surplus of CAMICO Mutual Insurance Company (the Company) as of December 31, 2009 and 2008, and the related statutory-basis statements of operations, changes in policyholders' surplus, and cash flow 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 auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 2 to the financial statements, the Company presents its financial statements in conformity with accounting practices prescribed or permitted by the California Department of Insurance, which practices differ from U.S. generally accepted accounting principles. The variances between such practices and U.S. generally accepted accounting principles are described in Note 2. The effects on the financial statements of these variances are not reasonably determinable but are presumed to be material.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with U.S. generally accepted accounting principles, the financial position of the Company at December 31, 2009 and 2008, or the results of its operations or its cash flow for the years then ended.

However, in our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CAMICO Mutual Insurance Company at December 31, 2009 and 2008, and the results of its operations and its cash flow for the years then ended in conformity with accounting practices prescribed or permitted by the California Department of Insurance.



May 4, 2010

## CAMICO Mutual Insurance Company

### Statements of Admitted Assets, Liabilities and Policyholders' Surplus – Statutory Basis

	<b>December 31</b>	
	<b>2009</b>	<b>2008</b>
	<i>(In Thousands)</i>	
<b>Admitted assets</b>		
Cash and invested assets:		
Bonds, at amortized cost (fair value: 2009 – \$124,340; 2008– \$132,236)	\$ 122,031	\$ 136,670
Equity securities, at fair value (cost: 2009 – \$10; 2008 – \$10,737)	10	9,191
Other invested assets, at fair value (cost: 2009 – \$3,320; 2008 – \$3,000)	4,106	2,602
Cash and short-term investments, at cost, which approximates fair value	15,106	3,761
Total cash and invested assets	141,253	152,224
Accrued interest receivable	1,242	1,497
Reinsurance recoverable on paid losses and loss adjustment expenses	758	1,190
Deferred tax asset, net	2,709	4,811
Premiums receivable	4,151	5,736
Federal income tax recoverable	2,347	1,452
Other assets	1,252	1,634
Total admitted assets	\$ 153,712	\$ 168,544
<b>Liabilities and policyholders' surplus</b>		
Liabilities:		
Reserves:		
Losses	\$ 51,605	\$ 57,005
Loss adjustment expenses	25,673	30,728
Unearned premiums	7,251	19,251
Total reserves	84,529	106,984
Premiums paid in advance	3,625	4,689
Accounts payable and accrued expenses	591	753
Ceded reinsurance premium	29,193	15,184
Other liabilities	3,668	5,818
Total liabilities	121,606	133,428
Commitments and contingencies <i>(Note 11)</i>		
Policyholders' surplus:		
Surplus notes	10,000	10,000
Unassigned surplus	22,106	25,116
Total policyholders' surplus	32,106	35,116
Total liabilities and policyholders' surplus	\$ 153,712	\$ 168,544

*See accompanying notes.*

CAMICO Mutual Insurance Company

Statements of Operations – Statutory Basis

	<b>Year Ended December 31</b>	
	<b>2009</b>	<b>2008</b>
	<i>(In Thousands)</i>	
Underwriting income:		
Premiums written	\$ <b>60,751</b>	\$ 76,297
Reinsurance ceded	<b>(43,401)</b>	(25,642)
Change in unearned premiums	<b>11,999</b>	(1,322)
Net premiums earned	<b>29,349</b>	49,333
Losses incurred	<b>13,364</b>	26,283
Loss adjustment expenses incurred	<b>16,669</b>	24,313
Other underwriting expenses incurred	<b>11,917</b>	18,680
Underwriting loss	<b>(12,601)</b>	(19,943)
Net investment income	<b>4,687</b>	6,470
Net realized capital gains (losses) net of federal income taxes of \$0 and \$(225) for 2009 and 2008, respectively	<b>2,158</b>	(661)
Gain on disposition of fixed assets	–	11
Loss after tax on capital gains (losses) and before all other federal income taxes	<b>(5,756)</b>	(14,123)
Federal income tax benefit	<b>(2,298)</b>	(1,094)
Net loss	<b>\$ (3,458)</b>	\$ (13,029)

*See accompanying notes.*

CAMICO Mutual Insurance Company

Statements of Changes in Policyholders' Surplus –  
Statutory Basis

Years Ended December 31, 2009 and 2008

	<b>Total Policyholders' Surplus</b>
	<i>(In Thousands)</i>
Balance at January 1, 2008	\$ 50,978
Net loss	(13,029)
Decrease in net unrealized capital gain on securities, net of tax of \$1,874	(3,676)
Increase in nonadmitted assets <i>(Note 14)</i>	(3,650)
Increase in net deferred tax asset <i>(Note 6)</i>	4,191
Other surplus adjustments	302
Balance at December 31, 2008	<u>35,116</u>
Net loss	<b>(3,458)</b>
Increase in net unrealized capital gain on securities, net of tax of \$873	<b>1,696</b>
Increase in nonadmitted assets <i>(Note 14)</i>	<b>(1,823)</b>
Increase in net deferred tax asset <i>(Note 6)</i>	<b>585</b>
Other surplus adjustments	<b>(10)</b>
Balance at December 31, 2009	<u><u>\$ 32,106</u></u>

*See accompanying notes.*

## CAMICO Mutual Insurance Company

### Statements of Cash Flow – Statutory Basis

	<b>Year Ended December 31</b>	
	<b>2009</b>	<b>2008</b>
	<i>(In Thousands)</i>	
<b>Operating activities</b>		
Premiums collected, net of reinsurance	\$ 31,910	\$ 57,474
Losses and loss adjustment expenses paid, net of reinsurance	(40,056)	(39,518)
Underwriting expenses paid	(12,033)	(20,248)
Investment income received	5,266	6,901
Federal income taxes recovered	1,403	400
Net cash (used in) provided by operating activities	<u>(13,510)</u>	5,009
<b>Investing activities</b>		
Proceeds from sales, maturities, or repayments of investments:		
Sales, maturities or repayments of bonds	71,769	31,615
Sales of equity securities	10,731	1,565
Other	107	969
Total investment proceeds	<u>82,607</u>	34,149
Cost of investments acquired:		
Purchases of bonds	(55,378)	(31,056)
Purchases of equity securities	(85)	(4,686)
Purchases of other invested assets	(320)	–
Total investments acquired	<u>(55,783)</u>	(35,742)
Net cash provided by (used in) investing activities	<u>26,824</u>	(1,593)
<b>Financing and miscellaneous activities</b>		
Other	(1,969)	(1,277)
Net cash used in financing and miscellaneous activities	<u>(1,969)</u>	(1,277)
Net change in cash and short-term investments	<b>11,345</b>	2,139
Cash and short-term investments, beginning of year	<b>3,761</b>	1,622
Cash and short-term investments, end of year	<u><u>\$ 15,106</u></u>	<u><u>\$ 3,761</u></u>

*See accompanying notes.*

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements

December 31, 2009

(Dollars in Thousands)

### **1. Organization**

CAMICO Mutual Insurance Company (the Company or CAMICO) offers professional liability and employment practices liability insurance (EPLI) to certified public accountants on a claims-made basis. The Company specializes in insuring certified public accounting (CPA) practices with limited or no Securities and Exchange Commission engagements, initial public offerings, or large company audit work. The Company is licensed to write professional liability insurance in 45 states and Washington, D.C. and EPLI in 45 states and Washington, D.C. For the years ended December 31, 2009 and 2008, the Company's California business represented 51% and 44%, respectively, of its total premiums written.

The Company has a wholly owned subsidiary, CAMICO Services, Inc. (CSI), dba CAMICO Insurance Services, which operates as an agent intermediary providing excess, and surplus lines capacity and insurance products for CPA firms underwritten by other insurance companies.

Effective July 1, 2009, CSI formed a new program with Liberty Insurance Underwriters, Inc. (LIU), a division of Liberty Mutual Group. The new program is administered by CSI with coverage provided by LIU and focuses primarily on professional liability policies with limits of \$3,000 or greater. Effective July 1, 2009, current and new CAMICO policyholders with limits of \$3,000 and above are written with LIU. In 2009, premiums of \$11,400 were written by LIU through this new program.

CSI receives a commission from LIU to cover acquisition, underwriting, and claims handling and general operating costs. In addition, CSI may share in profits of up to 5% of earned premium, in accordance with the Program Administrator Agreement.

The Company operates under a cost sharing agreement with CSI. In accordance with the agreement, CSI reimbursed the Company for expenses incurred in the amount of \$1,075 for the year ended December 31, 2009.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies

#### Basis of Presentation

The accompanying financial statements of the Company have been prepared in conformity with accounting practices prescribed or permitted by the California Department of Insurance (statutory basis of accounting). Such practices vary from U.S. generally accepted accounting principles (GAAP). The more significant variances from GAAP are as follows:

*Investments:* Investments in bonds are reported at amortized cost or fair value based on their National Association of Insurance Commissioners' (NAIC) rating; for GAAP, such fixed maturity investments would be designated at purchase as held-to-maturity, trading, or available-for-sale. Held-to-maturity fixed investments would be reported at amortized cost, and the remaining fixed maturity investments would be reported at fair value with unrealized holding gains and losses reported in operations for those designated as trading and as a separate component of surplus for those designated as available-for-sale. Fair value for statutory purposes is based on the price published by the Securities Valuation Office of the NAIC (SVO), if available, whereas fair value for GAAP is based on quoted market prices.

All single class and multi-class mortgage-backed/asset-backed securities (e.g., CMOs) are adjusted for the effects of changes in prepayment assumptions on the related accretion of discount or amortization of premium of such securities using either the retrospective or prospective methods. If it is determined that a decline in fair value is other-than-temporary, the cost basis of the security is written down to the undiscounted estimated future cash flows.

For GAAP purposes, all securities, purchased or retained, that represent beneficial interests in securitized assets (e.g., CMO, CBO, CDO, CLO, MBS and ABS securities), other than high credit quality securities, are adjusted using the prospective method when there is a change in estimated future cash flows. If it is determined that a decline in fair value is other-than-temporary, the cost basis of the security is written down to fair value. If high credit quality securities are adjusted, the retrospective method is used.

*Subsidiary:* The accounts and operations of CSI are not consolidated with the accounts and operations of the Company as would be required under GAAP. Equity in earnings of the Company's subsidiary is accounted for as a change in unrealized capital gains or losses. For GAAP, these earnings are accounted for as a component of net income.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies (continued)

*Policy Acquisition Costs:* The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.

*Nonadmitted Assets:* Certain assets designated as “nonadmitted,” principally net deferred tax assets, past-due premiums receivable, furniture and equipment, unsecured loans or cash advances to officers or agents, and other assets not specifically identified as an admitted asset within the NAIC’s Accounting Practices and Procedures Manual are excluded from the accompanying statements of admitted assets, liabilities and policyholders’ surplus and are charged directly to unassigned surplus. Under GAAP, such assets are included in the balance sheet, net of any applicable allowances.

*Reinsurance:* Any reinsurance balance amounts deemed to be uncollectible are written off through a charge to operations. In addition, a liability for reinsurance balances is provided for unsecured unearned premiums and unpaid losses ceded to reinsurers unauthorized to assume such business and for certain overdue reinsurance balances. Changes to those amounts are credited or charged directly to unassigned surplus. Under GAAP, an allowance for amounts deemed uncollectible would be established through a charge to earnings.

Reserves for losses and loss adjustment expenses and unearned premiums ceded to reinsurers have been reported as reductions of the related reserves rather than as assets as would be required under GAAP.

*Deferred Income Taxes:* Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining adjusted gross deferred tax assets expected to be realized within one year of the balance sheet date or 10% of policyholders’ surplus excluding any net deferred tax assets, EDP equipment and operating software and any net positive goodwill, plus 3) the amount of remaining adjusted gross deferred tax assets that can be offset against existing gross deferred tax liabilities, while considering the character (i.e., ordinary versus capital) of the deferred tax assets and liabilities. The remaining deferred tax assets are nonadmitted.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies (continued)

Effective in 2009, if certain requirements are met, the Company may elect to admit deferred tax assets in an amount equal to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a time frame corresponding with the IRS tax loss carryback provisions, not to exceed three years, plus 2) the lesser of the remaining amount of adjusted gross deferred tax assets expected to be realized within three years of the balance sheet date or 15% of policyholders' surplus excluding any net deferred tax assets, EDP equipment and operating system software and any net positive goodwill, plus 3) the amount of remaining adjusted gross deferred tax assets that can be offset against existing gross deferred tax liabilities, while considering the character (i.e., ordinary versus capital) of the deferred tax assets and liabilities. The Company did not meet the necessary requirements and, therefore, the method of determining the Company's admitted net deferred tax assets remained consistent with the prior year.

Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes are included in the computation of deferred taxes, a deferred tax asset is recorded for the amount of gross deferred tax assets expected to be realized in all future years, and a valuation allowance is established for deferred tax assets not realizable.

*Policyholder Dividends:* Policyholder dividends are recognized when declared rather than over the term of the related policies, as would be required under GAAP.

*Surplus Notes:* Surplus notes are reported as surplus rather than as liabilities. Additionally, interest on surplus notes is recognized when approved for payment by the Department rather than accrued based on the outstanding balance reported under GAAP.

*Guaranty Fund and Other Assessments:* A liability for guaranty fund and other assessments (net of certain offsets depending on state rules) is accrued after an insolvency has occurred regardless of whether the assessment is based on premiums written before or after the insolvency. Under GAAP, the assessment recognized is typically accrued when premiums are written because the assessment generally is based on prospective premium writings.

*Statements of Cash Flow:* Cash and short-term investments in the statements of cash flow represent cash balances and investments with initial maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents includes cash balances and investments with initial maturities of three months or less.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **2. Summary of Significant Accounting Policies (continued)**

The effects of the foregoing variances from GAAP on the accompanying statutory-basis financial statements have not been determined, but are presumed to be material.

#### **Use of Estimates**

The preparation of financial statements of insurance companies requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future, as more information becomes known, which could impact the amounts reported and disclosed herein.

#### **Cash and Short-Term Investments**

Cash and short-term investments include demand deposits and money market funds. The carrying amount of these assets approximates fair value.

Short-term investments include investments with remaining maturities of one year or less at the time of acquisition and are principally stated at cost, which approximates fair value.

#### **Investments**

Investments are stated at valuation rates prescribed by, or deemed acceptable to, the NAIC. Bonds not backed by other loans are stated at amortized cost using the interest method, except bonds that are defined by the NAIC as non-investment grade (class 3-6), which are stated at the lower of amortized cost or fair value. Under NAIC guidelines, when market value rates are not available for bonds, fair value is stated at amortized cost. Equity securities of unaffiliated entities are carried at fair value as determined by the SVO. Realized gains or losses on the sale of bonds are determined based on the specific amortized cost of the investments sold and are included in operations. Realized gains or losses on the sale of equity securities are based on the specific-identification method and are included in operations. Unrealized gains and losses from revaluation of equity securities are reflected in policyholders' surplus.

The Company's wholly owned subsidiary, CSI, is reported at its underlying equity.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **2. Summary of Significant Accounting Policies (continued)**

The Company reviews its investment portfolio for reductions in fair value below cost that, in the opinion of the Company, represent a permanent or other-than-temporary impairment (OTTI). Declines in fair value of investments deemed to be other than temporarily impaired or permanently impaired are accounted for as a realized loss in the statement of operations. Subsequent recoveries in fair value of equity securities previously deemed other than temporarily impaired are reflected as unrealized gains and are included as a component of surplus. At December 31, 2009 and 2008, the Company held investments that incurred other-than-temporary impairment of \$317 and \$107, respectively.

Loan-backed bonds and structured securities are stated at amortized cost using the retrospective method. Under this method, amortized value is calculated based on the present value of future cash flows, using an assumed prepayment rate. Prepayment assumptions are obtained from broker-dealer survey values.

The Company has minor ownership interests in a limited partnership (Archipelago Partners, L.P.). The Company carries this investment at fair value based on its interest in the underlying audited GAAP equity of the investee, with unrealized gains and losses reported in unassigned surplus. The Company did not recognize any other-than-temporary impairment write-down for its investment in the limited partnership during the years ended December 31, 2009 and 2008. The investment is reflected as other invested assets in the accompanying statements of admitted assets, liabilities and policyholders' surplus.

### **Premiums**

Premiums written are earned on a daily pro rata basis over the policy term. Unearned written premiums are reported as unearned premiums in the accompanying statements of admitted assets, liabilities and policyholders' surplus. In 2009 and 2008, 35% and 34%, respectively, of the policies were written on a calendar year.

A provision for "free" extended reporting endorsement coverage for certain policyholders due to death, disability, or retirement has been recorded as unearned premiums. These premiums are earned upon the death, disability, or retirement of a policyholder. The Company recorded related estimated unearned premiums of \$1,688 and \$1,634 as of December 31, 2009 and 2008, respectively, for this coverage and \$57 and \$85 were recognized as earned premiums for the years ended December 31, 2009 and 2008, respectively. The unearned premium reserve reflects the Company's best estimate of the future death, disability, and retirement benefits.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **2. Summary of Significant Accounting Policies (continued)**

For uncollected premiums receivable, after the calculation of nonadmitted amounts, an evaluation is made of the remaining admitted assets to determine if there is an impairment and an allowance is established.

#### **Loss and Loss Adjustment Expenses**

Loss and loss adjustment expense reserves represent management's best estimate of the ultimate net cost of all reported and unreported losses incurred through December 31. The Company does not discount loss and loss adjustment expense reserves. The reserves for unpaid losses and loss adjustment expenses are estimated using individual case-basis valuations and statistical analyses. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes the reserves for losses and loss adjustment expenses are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations.

Salvage and subrogation recoverables are estimated using the "case basis" method. Recoverable amounts deducted from the liability for losses and loss adjustment expenses were \$670 and \$1,100 at December 31, 2009 and 2008, respectively.

#### **Premium Deficiency Reserves**

Premium deficiency reserves are established for the amount of the anticipated losses, loss adjustment expenses, commissions and other acquisition costs and maintenance costs that have not previously been expensed in excess of the recorded unearned premium reserve and future installment premiums on existing policies. There were no premium deficiency reserves at December 31, 2009 and 2008, respectively.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies (continued)

#### Reinsurance

Reinsurance recoverables on paid losses and loss adjustment expenses (LAE) are reported as assets. Estimated reinsurance receivables on unpaid losses and LAE are recognized in a manner consistent with the liabilities relating to the underlying reinsured contract. Excess of loss insurance premiums, prepaid reinsurance premiums and losses and loss adjustment expenses ceded to reinsurers have been reported as reductions of written premiums, unearned premiums and losses and loss adjustment expenses, respectively.

#### Electronic Data Processing Equipment, Furniture and Other

The admitted portion of electronic data processing (EDP) equipment is limited to 3% of capital and surplus (adjusted for EDP). The admitted portion is reported at cost, less accumulated depreciation, in other assets. Electronic data processing equipment, operating software, and nonoperating software are depreciated using the straight-line method over three years.

The balances by major category of depreciable EDP assets are summarized as follows:

	Acquisition Cost	Accumulated Depreciation	Net
At December 31, 2009:			
EDP hardware	\$ 1,087	\$ (942)	\$ 145
EDP software	2,250	(1,437)	813
Total EDP	\$ 3,337	\$ (2,379)	958
Nonadmitted EDP			(813)
Net admitted EDP			\$ 145
At December 31, 2008:			
EDP hardware	\$ 1,034	\$ (738)	\$ 296
EDP software	1,856	(1,121)	735
Total EDP	\$ 2,890	\$ (1,859)	1,031
Nonadmitted EDP			(735)
Net admitted EDP			\$ 296

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **2. Summary of Significant Accounting Policies (continued)**

Leasehold improvements are carried at cost less accumulated amortization. The Company provides for amortization of leasehold improvements using the straight-line method over the lesser of the useful life of the asset or the remaining original lease term, excluding options or renewal periods.

Other furniture and equipment is depreciated using the straight-line method over five to seven years.

Depreciation and amortization expense charged to operations for the years ended December 31, 2009 and 2008, was \$631 and \$647, respectively.

Maintenance and repairs are charged to expense as incurred.

### **Net Investment Income**

Net investment income primarily represents interest and dividends received or accrued on bonds and equity securities. It also includes amortization of any purchase premium or accretion of purchase discount using the interest method, adjusted prospectively for any change in estimated yield-to-maturity. Net investment income is reduced by investment management expenses and interest expense from the issuance of surplus notes.

### **Deferred Taxes**

Changes in deferred tax assets and liabilities related to changes in unrealized gains and losses on investments are reported as a component of changes in unrealized capital gains and losses in the statements of changes in policyholders' surplus. Other changes in deferred tax assets and liabilities are direct adjustments to surplus and are reported separately in the statements of changes in policyholders' surplus.

### **Concentration of Credit Risk**

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist of temporary cash investments, fixed maturity securities and reinsurance recoverable on paid and unpaid losses.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies (continued)

The Company places its temporary cash investments with high credit quality financial institutions. Concentrations of credit risk with respect to fixed maturity securities are limited due to the large number of such investments and their distribution across many different industries and geographic regions. To minimize its exposure to significant losses from reinsurance insolvencies, the Company evaluates the financial condition of its reinsurers and reinsures its business with highly rated reinsurers.

#### New Accounting Standards

In September 2009, the NAIC adopted Statutory Statement of Accounting Principles (SSAP) No. 43 – Revised, *Loan-backed and Structured Securities*, which supersedes SSAP No. 98, *Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP 43* (SSAP No. 43(R)), which revises SSAP No. 43 and supersedes SSAP No. 98. The primary revisions to existing guidance promulgated by SSAP No. 43(R) relate to the determination, measurement and recognition of other-than-temporary impairments on loan-backed and structured securities and the determination of carrying value method and final NAIC designation on securities subject to multiple designations. SSAP No. 43(R) did not have an impact upon adoption on the Company's financial position or results of operations. The additional disclosures required by SSAP No. 43(R) have been included in Note 4.

In December 2009, the NAIC approved revisions to SSAP No. 9, *Subsequent Events*, which are effective for years ending on or after December 31, 2009. The revisions require companies to evaluate subsequent events through the date that the financial statements are available to be issued and to disclose such date in the notes to the financial statements. Management of CAMICO has evaluated all events occurring after December 31, 2009 through May 4, 2010, the date the financial statements were available to be issued, to determine whether any event required either recognition or disclosure in the financial statements.

In December 2009, the NAIC adopted SSAP No. 10 – Revised, *Income Taxes* (SSAP No. 10(R)), which revises SSAP No. 10. SSAP No. 10(R) increases the admissibility limits of deferred tax assets if certain risk-based capital thresholds are met. The revision also incorporates the requirement for a valuation allowance if it is more likely than not that some or all of a gross deferred tax asset will not be realized. The revisions, including additional required disclosures are effective for 2009 annual financial statements and 2010 interim and annual financial statements only. CAMICO adopted SSAP No. 10(R) in 2009, however, the adoption did not have a material impact on the Company's financial statements.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 2. Summary of Significant Accounting Policies (continued)

In December 2009, the NAIC adopted SSAP No. 100, *Fair Value Measurements* (SSAP No. 100). This standard defines fair value, establishes a framework for measuring fair value, and establishes disclosure requirements about fair value. The Company adopted SSAP No. 100 in 2009. Refer to Note 3 for the required disclosures.

### 3. Fair Value Measurements

Included in various investment related line items in the financial statements are certain financial instruments carried at fair value. Other financial instruments are periodically measured at fair value, such as when impaired, or, for certain bonds when carried at the lower of cost or market. Fair values are based on quoted market prices when available. When market prices are not available, fair value is generally estimated using discounted cash flow analyses, incorporating current market inputs for similar financial instruments with comparable terms and credit quality (matrix pricing). In instances where there is little or no market activity for the same or similar instruments, the Company estimates fair value using methods, models and assumptions that management believes market participants would use to determine a current transaction price. These valuation techniques involve some level of management estimation and judgment which becomes significant with increasingly complex instruments or pricing models. Where appropriate, adjustments are included to reflect the risk inherent in a particular methodology, model or input used.

The Company's financial assets and liabilities carried at fair value have been classified, for disclosure purposes, based on a hierarchy defined by SSAP No. 100. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). An asset's or a liability's classification is based on the lowest level input that is significant to its measurement. For example, a Level 3 fair value measurement may include inputs that are both observable (Levels 1 and 2) and unobservable (Level 3). The levels of the fair value hierarchy are as follows:

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 3. Fair Value Measurements (continued)

*Level 1* – Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.

*Level 2* – Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.

*Level 3* – Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the Company’s best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

The Company’s financial assets measured at fair value on a non-recurring basis are summarized in the following table as of December 31, 2009.

<u>Description</u>	<u>Fair Value</u>			<u>Total Fair Value</u>	<u>Total Impairment</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>		
Bonds	\$ 1,664	\$ –	\$ –	\$ 1,664	\$ 317

The Company’s financial assets measured at fair value on a recurring basis as of December 31, 2009 included other invested assets in the amount of \$4,106. This financial asset is classified as a Level 3 asset.

### 4. Investments

The Company’s investments in equity securities consist of the following at December 31:

	<u>2009</u>	<u>2008</u>
Mutual funds	\$ –	\$ 9,181
CAMICO Services, Inc.	10	10
	<u>\$ 10</u>	<u>\$ 9,191</u>

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 4. Investments (continued)

Gross unrealized gains and losses pertaining to investments in equity securities at December 31 are:

	<b>2009</b>	<b>2008</b>
Unrealized gains	\$ -	\$ -
Unrealized losses	-	(1,546)
Total	\$ -	\$ (1,546)

Proceeds from sales of investments in equity securities during 2009 were \$10,731. Gross and net losses of \$80 were realized on those sales. Proceeds from sales of investments in equity securities during 2008 were \$1,565. A gross and net loss of \$56 was realized on those sales.

Gross unrealized gains and losses pertaining to investments in other invested assets at December 31 are:

	<b>2009</b>	<b>2008</b>
Unrealized gains	\$ <b>786</b>	\$ -
Unrealized losses	-	(399)
Total	\$ <b>786</b>	\$ (399)

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 4. Investments (continued)

The amortized cost and fair value of investments in bonds are as follows:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
December 31, 2009				
U.S. Treasury and U.S. agency securities	\$ 6,557	\$ 424	\$ (179)	\$ 6,802
Obligations of states and political subdivisions	35,407	667	(665)	35,409
Corporate securities	72,656	2,194	(324)	74,526
Mortgage and asset-backed securities	7,868	82	(347)	7,603
	\$ 122,488	\$ 3,367	\$ (1,515)	\$ 124,340
December 31, 2008				
U.S. Treasury and U.S. agency securities	\$ 9,150	\$ 1,346	\$ –	\$ 10,496
Obligations of states and political subdivisions	55,831	892	(3,922)	52,801
Corporate securities	45,379	405	(2,299)	43,485
Mortgage and asset-backed securities	26,501	640	(1,687)	25,454
	\$ 136,861	\$ 3,283	\$ (7,908)	\$ 132,236

Cost or amortized cost may differ from the carrying value due to bonds that have a NAIC designation of three or greater and have a carrying value that is equal to the lower of the bonds' cost, amortized cost or fair value. At December 31, 2009 and 2008, the Company held bonds that had a NAIC designation of three or greater, which caused the carrying value of the bonds to be \$457 and \$191, respectively, less than the related cost or amortized cost.

Proceeds from sales of investments in bonds during 2009 were \$55,689. Gross gains of \$3,114 and gross losses of \$560 were realized on those sales. Proceeds from sales of investments in bonds during 2008 were \$21,071. Gross gains of \$734 and gross losses of \$696 were realized on those sales.

At December 31, 2009 and 2008, bonds with a carrying value of \$4,525 and \$4,582, respectively, were on deposit with regulatory authorities as required by law.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 4. Investments (continued)

The following table shows gross unrealized losses and fair values of bonds, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>December 31, 2009</b>						
Bonds:						
U.S. Treasury and U.S. agency securities	\$ 2,055	\$ (179)	\$ -	\$ -	\$ 2,055	\$ (179)
Obligations of states and political subdivisions	3,913	(99)	12,968	(566)	16,881	(665)
Corporate securities	20,183	(160)	5,009	(164)	25,192	(324)
Mortgage-backed securities						
U.S. government agencies	588	(26)	-	-	588	(26)
Corporate	-	-	3,688	(321)	3,688	(321)
<b>Total</b>	<b>\$ 26,739</b>	<b>\$ (464)</b>	<b>\$ 21,665</b>	<b>\$ (1,051)</b>	<b>\$ 48,404</b>	<b>\$ (1,515)</b>
<b>December 31, 2008</b>						
Bonds:						
U.S. Treasury and U.S. agency securities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Obligations of states and political subdivisions	10,783	(434)	16,532	(3,488)	27,315	(3,922)
Corporate securities	17,972	(1,225)	11,606	(1,074)	29,578	(2,299)
Mortgage-backed securities						
U.S. government agencies	3	-	3	-	6	-
Corporate	3,712	(725)	3,163	(962)	6,875	(1,687)
<b>Total</b>	<b>\$ 32,470</b>	<b>\$ (2,384)</b>	<b>\$ 31,304</b>	<b>\$ (5,524)</b>	<b>\$ 63,774</b>	<b>\$ (7,908)</b>

The Company reviews at least quarterly its investment portfolio for securities that may have an other-than-temporary impairment in value. For any investment security deemed to be OTTI, the investment's amortized cost is written down to fair value with a realized loss recognized in operations. Based on a review of the bonds included in the table above, the Company determined that the unrealized losses were primarily a result of the interest rate environment and not the credit quality of the issuers. In December 2009, the Company impaired three mortgage-backed securities due to credit exposure and expectation that the collection of all contractual cash flows is not probable and recognized a loss of \$237.

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 4. Investments (continued)

In accordance with SSAP No. 43(R), these impairment charges were recorded as the present value of cash flows expected to be collected was less than the amortized cost basis of each security. The following table summarizes each loan-backed security for which an other-than-temporary impairment charge was recognized.

CUSIP	Description	Amortized Cost Prior to Current Period Other- Than-Temporary Impairment	OTTI Recognized in Earnings	Fair Value	Amortized Cost After Current Period Other- Than-Temporary Impairment
3622N6AA7	GSR Mortgage Loan Trust	\$466	\$(79)	\$306	\$387
05946XYZ0	Banc of America Fund	550	(106)	381	444
36185MBJ0	GMAC Mortgage Corp	598	(52)	469	546

In total, the Company recognized a loss of \$317 on impaired securities in 2009. As of December 31, 2008, the Company identified one impaired corporate bond and a write-down of \$107 was recognized as a realized loss.

The Company believes that all remaining unrealized losses on individual securities are the result of normal price fluctuations due to market conditions and interest rates and are not an indication of an other-than-temporary impairment.

The amortized cost and fair value of bonds at December 31, 2009, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due in one year or less	\$ 5,072	\$ 5,183
Due after one year through five years	64,110	65,574
Due after five years through ten years	35,923	36,721
Due after ten years	9,515	9,259
Mortgage and asset-backed securities	7,868	7,603
	<u>\$ 122,488</u>	<u>\$ 124,340</u>

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 5. Other Liabilities

Other liabilities consist primarily of accrued and deferred compensation, deferred rent and certain employee benefits as shown below as of December 31:

	2009	2008
Accrued and deferred compensation	\$ 372	\$ 289
Accrued employee benefits	840	3,146
Deferred fees	1,169	1,179
Premium taxes, licenses, and fees payable	14	364
Deferred rent	70	172
Miscellaneous liabilities	1,203	668
	\$ 3,668	\$ 5,818

#### 6. Federal Income Taxes

The Company files a consolidated federal income tax return with its wholly owned subsidiary, CSI. The method of allocation between the companies has been formalized in a written tax allocation agreement. Allocation is based upon separate return calculations with current credit given for net losses and/or credits that result in an actual reduction in the tax liability of the consolidated group.

The components of the net deferred tax asset at December 31 are as follows:

Description	December 31					
	2009			2008		
	Ordinary	Capital	Total	Ordinary	Capital	Total
Gross deferred tax assets	\$ 10,285	\$ 182	\$ 10,467	\$ 9,885	\$ 698	\$ 10,583
Statutory valuation allowance	-	-	-	-	-	-
Adjusted gross deferred tax assets	10,285	182	10,467	9,885	698	10,583
Gross deferred tax liabilities	(727)	(267)	(994)	(822)	-	(822)
Net deferred tax asset (liability) before admissability test	\$ 9,558	\$ (85)	\$ 9,473	\$ 9,063	\$ 698	\$ 9,761

The Company did not meet the requirements to admit additional deferred tax assets pursuant to SSAP 10R, paragraph 10(e). Therefore, the current year election was the same as the prior year.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 6. Federal Income Taxes (continued)

The amount of each component of admitted deferred tax asset, by tax character, admitted pursuant to:

	December 31					
	2009			2008		
SSAP No. 10R Paragraph 10	Ordinary	Capital	Total	Ordinary	Capital	Total
<b>Admitted pursuant to 10.a –</b>						
Temporary difference reversing in one year limited to federal income taxes recoverable through loss carryback	\$ –	\$ –	\$ –	\$ –	\$ –	\$ –
Adjusted gross deferred tax asset expected to be realized in one year per 10.b.i. – One-year reversals remaining after loss carryback limitation	\$ 2,555	\$ 182	\$ 2,737	\$ 4,148	\$ 663	\$ 4,811
OR						
10% of adjusted capital and surplus limit per 10.b.ii	2,527	182	2,709	4,435	663	5,098
<b>Admitted pursuant to 10.b</b> (lesser of 10.b.i or 10.b.ii)	\$ 2,527	\$ 182	\$ 2,709	\$ 4,148	\$ 663	\$ 4,811
<b>Admitted pursuant to 10.c. –</b> remaining deferred tax assets to be offset against deferred tax liabilities	\$ 727	\$ 267	\$ 994	\$ 822	\$ –	\$ 822
Total admitted deferred tax asset (total of 10.a.,b.,c.)	3,254	449	3,703	4,970	663	5,633
Total gross deferred tax liabilities	(727)	(267)	(994)	(822)	–	(822)
Net admitted deferred tax asset	\$ 2,527	\$ 182	\$ 2,709	\$ 4,148	\$ 663	\$ 4,811
Non-admitted deferred tax assets	\$ 6,764	\$ –	\$ 6,764	\$ 4,950	\$ –	\$ 4,950

Current income tax consists of the following components for the years ended December 31:

	2009	2008
Current portion of tax provision	\$ (2,298)	\$ (1,054)
Decrease of prior periods' tax provisions	–	(40)
Federal income tax benefit on ordinary income	(2,298)	(1,094)
Federal income tax benefit on net capital losses	–	(225)
Federal income tax benefit	\$ (2,298)	\$ (1,319)

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 6. Federal Income Taxes (continued)

The current tax benefit in 2009 is due to carrying back net operating losses and amending tax returns accordingly for 2003, 2004 and 2005.

The components of the net deferred tax assets at December 31 are as follows:

	<b>2009</b>	<b>2008</b>	<b>Change</b>	<b>Category</b>
Deferred tax assets:				
Net operating loss carryforward	\$ 6,082	\$ 4,190	\$ 1,892	Ordinary
Discounting of unpaid losses and loss adjustment expenses	1,857	2,075	(218)	Ordinary
Compensation accruals	798	1,225	(427)	Ordinary
Change in unearned premiums	493	1,309	(816)	Ordinary
Nonadmitted assets	590	1,012	(422)	Ordinary
Advance premiums	247	319	(72)	Ordinary
Minimum tax credit	11	110	(99)	Ordinary
Other	389	343	46	Ordinary
<b>Total deferred tax assets</b>	<b>10,467</b>	<b>10,583</b>	<b>(116)</b>	
Nonadmitted deferred tax assets	6,764	4,950	1,814	
Admitted deferred tax assets	3,703	5,633	(1,930)	
Deferred tax liabilities:				
Unrealized gains	267	-	267	Capital
Other	373	411	(38)	Ordinary
Premium acquisition expenses	339	339	-	Ordinary
Bond market discount	15	72	(57)	Ordinary
<b>Total deferred tax liabilities</b>	<b>994</b>	<b>822</b>	<b>172</b>	
<b>Net admitted deferred tax asset</b>	<b>\$ 2,709</b>	<b>\$ 4,811</b>	<b>\$ (2,102)</b>	

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 6. Federal Income Taxes (continued)

The change in net deferred income taxes at December 31 is comprised of the following:

	2009	2008	Change
Total deferred tax assets	\$ 10,467	\$ 10,583	\$ (116)
Total deferred tax liabilities	(994)	(822)	(172)
Net deferred tax assets	\$ 9,473	\$ 9,761	(288)
Tax effect of increase in net unrealized capital gain on securities			873
Increase in net deferred tax asset			\$ 585

The provision for federal income tax is different from that which would be computed by applying the statutory federal income tax rate to income before tax as follows for the year ended December 31:

	2009		2008	
Federal income tax at statutory rate	\$ (1,957)	34.0%	\$ (4,878)	34.0%
Increase (decrease) due to:				
Tax-exempt interest	(602)	10.5%	(692)	4.8
Change in nonadmitted assets	(271)	6.0%	(81)	0.6
Dividend received	-	-	(32)	0.2
Other	(53)	0.6%	173	(1.2)
Total statutory income tax expense	\$ (2,883)	51.1%	\$ (5,510)	38.4%
Federal income tax rate	\$ (2,298)	39.9%	\$ (1,319)	9.2%
Increase in net deferred tax asset	(585)	11.2%	(4,191)	29.2
Total statutory income tax expense	\$ (2,883)	51.1%	\$ (5,510)	38.4%

At December 31, 2009, the Company has \$17,888 of net operating loss carryforwards available until 2029 to offset against future taxable income.

The Company does not have any federal income taxes incurred in the current or prior year that will be available for recoupment in the event of future net losses.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 6. Federal Income Taxes (continued)

On January 1, 2009, the Company adopted new accounting guidance for uncertain tax positions. As of December 31, 2009, the Company has no uncertain tax positions, and therefore has not recorded a contingent liability. There were no tax positions for which management believes it is reasonably possible that the total amount of tax contingencies will significantly increase or decrease within 12 months of the reporting date.

As of December 31, 2009, the only material jurisdiction the Company is subject to examination in is the U.S. federal jurisdiction for the tax years 2006 through the present.

### 7. Other Assets

Other assets include deductible/copy receivables, electronic data processing equipment and other miscellaneous receivables as shown below:

	<u>2009</u>	<u>2008</u>
Deductibles billed to policyholders	\$ 898	\$ 308
Electronic data processing equipment	145	312
Receivable for shared facilities	136	88
Miscellaneous receivables	73	926
	<u>\$ 1,252</u>	<u>\$ 1,634</u>

### 8. Reinsurance

The Company, in the normal course of its business, reinsures certain risks with other companies through contractual agreements. Such arrangements serve to limit the Company's loss on large claims in any single risk. Risks reinsured would become a liability of the Company in the event any reinsurer is unable to or will not fulfill the obligations assumed under the agreements. Certain reinsurance agreements contain provisions for adjustments based on loss experience of the contracts. Such adjustments are recorded on an accrual basis, and are initially settled with reinsurers three years after the contract period with annual adjustments thereafter. Contracts entered into after June 1, 2006, are generally settled with reinsurers within sixty (60) days of the termination of the contract. There are provisions in the contracts that allow for the runoff of the treaty at the Company's discretion. From June 1, 2008, the Company retains the first \$1,000 of each and every professional liability claim. The employment practices claims are on a 50% quota

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 8. Reinsurance (continued)

share basis from dollar one. The Company entered into a 47.5% quota share treaty with Hannover Re, Ireland (Quota Share Treaty), on new and renewal policies effective January 1, 2009 for calendar year 2009. For calendar year 2009, the net effect of the Quota Share Treaty was to reduce the maximum retained loss to \$525.

A summary of current reinsurance contract terms is as follows:

Effective July 1, 2009, the Company entered into an agreement with LIU for policies with limits greater than \$3,000, as discussed in Note 1, to reduce its policy limit exposure. For the period of July 1, 2009 to December 31, 2009, the Company entered into an excess of loss treaty ceding losses in excess of \$1,000 up to a total of \$1,000 per claim. From July 1, 2009 to December 31, 2009, the maximum retained loss was \$1,000 per claim (subject to the 47.5% Quota Share Treaty). All other losses are ceded and the maximum coverage per policy is provided by a negotiated reinsurance treaty program and facultative reinsurance placements. The primary treaty covers all losses that exceed retention up to a total of \$1,000 per claim.

For claims made and reported to the Company for policies issued between the month of June 1, 2009 to June 30, 2009, the Company ceded all losses in excess of \$1,000 on a facultative basis.

For claims made and reported to the Company from June 1, 2009 to December 31, 2009, the Company had reinsurance over and above the underlying limits, inclusive of any facultative reinsurance, of \$10,000 in limits for each and every claim for losses in excess of policy limits and or extra contractual obligations. This coverage is subject to a 10% co-pay.

For claims made and reported to the Company from January 1, 2009 to May 31, 2009, the maximum retained loss was \$1,000 per claim. This treaty is currently in run off. All losses in excess of \$1,000 are reinsured, with new and renewal business subject to the 47.5% Quota Share Treaty. For the period of June 1, 2008 to May 31, 2009, the Company entered into a primary reinsurance program that ceded 100% of the losses in excess of \$1,000 to a maximum of \$4,000. Twenty five percent (25.0%) of the program is on a funds held basis and is an addendum to the Aggregate Excess of Loss (Stop Loss) reinsurance agreement entered into on January 1, 2008 (Part B). The Company retained an annual aggregate deductible (AAD) of 9% of subject earned premium on 35% of the business. All other losses are ceded and the maximum coverage per policy is provided by a negotiated reinsurance treaty program and facultative reinsurance placements. The primary treaty covers all losses that exceed retention up to a total of \$5,000 per claim.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 8. Reinsurance (continued)

From January 1, 2009 through May 31, 2009, the Company had reinsurance over and above the underlying limits of \$5,000, inclusive of any facultative reinsurance, of \$10,000 in coverage each and every claim for losses in excess of policy limits and or extra contractual obligations. This coverage is subject to a 10% co-pay.

For claims made and reported to the Company from June 1, 2008 to December 31, 2008, the maximum retained loss was \$1,000 per claim. All losses in excess of \$1,000 are reinsured. The maximum coverage per policy is provided by negotiated reinsurance treaty programs and facultative reinsurance placements. The primary treaty covers all losses that exceed retention up to a total of \$5,000 per claim.

For claims made and reported to the Company from January 1, 2008 to May 31, 2008, the maximum retained loss was \$1,200 per claim. The Company retains 5% of each and every loss up to \$4,000 in excess of \$1,000 for an additional amount of up to \$200 at this layer. Additionally, the Company has an AAD of 9% of subject earned premium on 47.5% of the business. This agreement was terminated on May 31, 2008. All other losses are ceded and the maximum coverage per policy is provided by negotiated reinsurance treaty programs and facultative reinsurance placements. The primary treaty covers all losses that exceed retention up to a total of \$5,000 per claim.

From January 1, 2008 through December 31, 2008, the Company had reinsurance over and above the underlying limit of \$5,000, inclusive of any facultative reinsurance, of \$10,000 in limits for each and every claim for losses in excess of policy limits and or extra contractual obligations. This coverage is subject to a 10% co-pay.

Effective January 1, 2009, the Company entered into an aggregate excess of loss reinsurance agreement on a funds held basis to cede all losses in excess of the 2009 accident year loss ratio of 65.0%. Losses ceded under this agreement in 2009 were \$2,929, and net premiums ceded were \$2,912.

Effective January 1, 2008, the Company entered into an aggregate excess of loss reinsurance agreement (Part A) on a funds held basis to cede all losses in excess of the 2008 accident year loss ratio of 61.25%. Losses ceded under this agreement in 2009 were \$7,452. No losses were ceded under this agreement in 2008. Net premiums ceded in 2009 and 2008 were \$1,651 and \$3,323, respectively for this agreement.

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 8. Reinsurance (continued)

During 2009 and 2008, the Company continued the Employment Practices Liability Insurance (EPLI) quota share reinsurance agreement whereby 50% of the Company's EPLI business is ceded.

For the period of July 1, 2009 to December 31, 2009, 26 policies written in excess of \$2,000 were placed facultatively. For the period of June 2009, all policies with limits greater than \$1,000 were placed facultatively. For the period of January 1, 2009 to May 31, 2009 and for calendar year 2008, any individual policy with limits in excess of \$5,000, are placed facultatively.

The effects of reinsurance on premiums written and earned are as follows:

	2009		2008	
	Written	Earned	Written	Earned
Direct premiums	\$ 60,751	\$ 69,113	\$ 76,297	\$ 75,556
Ceded premiums	(43,401)	(39,764)	(25,642)	(26,223)
Net premiums	\$ 17,350	\$ 29,349	\$ 50,655	\$ 49,333

The Company's reinsurance agreements also contain a provision to reimburse acquisition costs through a ceding commission. Total ceding commission income reduced other underwriting expenses by \$9,250 and \$3,332 in 2009 and 2008, respectively. The ceding commission in 2009 included a quota share commission of \$5,028, which represents 26% of premiums written. The quota share agreement was not in effect in 2008.

Liabilities for unpaid losses and loss adjustment expenses, unearned premiums and incurred losses and loss adjustment expenses have been reduced by the following amounts for the effects of reinsurance ceded:

	2009	2008
Unpaid losses and loss adjustment expenses *	\$ 81,589	\$ 44,712
Unearned premiums *	7,376	3,739
Incurred losses and loss adjustment expenses	49,557	26,653

\*At December 31

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 8. Reinsurance (continued)

Unsecured reinsurance recoverables at December 31, 2009 that exceed 3% of the Company's surplus are summarized as follows:

Munich Reins America	\$10,564
Hannover Ruckversicherungs-Aktiengesellschaft	6,989
Aspen Insurance UK Ltd	6,889
Lloyd's Syndicate 2623	4,978
Lloyd's Syndicate 4472 (0190)	4,794
General Reinsurance Corp	4,737
White Mountain (Folksamerica) Reins Co	3,862
The Toa Reinsurance America	3,852
Axis Reinsurance Co	3,106
Transatlantic Reinsurance Co	2,365
Lloyd's Syndicate 0623	1,778

### 9. Policyholders' Surplus

In June 2005, the Company issued surplus notes to Preferred Term Securities XVII, Ltd. and First Tennessee Bank, N.A. in return for \$10,000 in cash. The surplus notes call for the Company to pay quarterly interest at a 7.65% annual rate for five years and at LIBOR plus 3.15% thereafter. Any payment of interest or repayment of principal is subject to approval by the California Department of Insurance. Claims under the surplus notes are subordinated and are paid out of any assets remaining after payment of all liabilities including senior claims and any senior indebtedness of the Company. Unrecorded interest expense of approximately \$32 at December 31, 2009, will be expensed and paid in March 2010 upon receipt of approval by the California Department of Insurance for such payment. The fair value of the surplus notes at December 31, 2009 and 2008, was \$10,173 and \$10,303, respectively.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 9. Policyholders' Surplus (continued)

A summary of the terms of the surplus notes follows:

Date Issued	Interest Rate	Par Value (Face Amount of Notes)	Carrying Value of Notes	Interest and/or Principal Paid Current Year	Total Interest and/or Principal Paid	Unapproved Interest and/or Principal Paid	Date of Maturity
June 3, 2005	5-Year Fixed @ 7.65% and thereafter @ LIBOR +3.15%	\$10,000	\$10,000	\$765	\$3,468	\$0	June 3, 2035

The maximum amount of dividends which can be paid by insurers, domiciled in the state of California to policyholders, without the prior approval of the Insurance Commissioner is subject to restrictions relating to statutory surplus.

Unassigned surplus at December 31, 2007, was \$40,978. The maximum dividend payment that could have been declared without prior approval in 2008 was the greater of (1) 10% of preceding year's unassigned surplus or \$4,098, or (2) preceding year's net income of \$826. No dividends were declared in 2008.

Unassigned surplus at December 31, 2008, was \$25,116. The maximum dividend payment that may be declared without prior approval in 2009 is the greater of (1) 10% of preceding year's unassigned surplus or \$2,511 or (2) preceding year net income of \$0. No dividends were declared in 2009.

Property/casualty insurance companies are subject to certain Risk-Based Capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property/casualty insurance company is determined based on the various risk factors related to it.

The Company reported Risk-Based Capital of 222.7% at December 31, 2009, and failed an RBC Trend Test under section 739.3 of the California Insurance Code. The Company failed the RBC Trend Test because its combined ratio of 171% is greater than 120% and the RBC percentage is between 200% and 300%. As a result, the California Department of Insurance is requiring the Company to provide monthly reporting in 2010. The Company passed all other RBC tests with total adjusted surplus (TAS) of \$32,107 at December 31, 2009 compared to Company Action Level Surplus of \$28,832 at December 31, 2009.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **9. Policyholders' Surplus (continued)**

At December 31, 2008, the Company reported Risk Based Capital of 228.3% and failed an RBC Trend Test. The Company failed the RBC Trend Test because its combined ratio of 138% was greater than 120% and the RBC percentage was between 200% and 300%. As a result, the California Department of Insurance required the Company to provide a comprehensive financial plan which was submitted on April 15, 2009, in addition to providing more frequent reporting for 2009. The Company passed all other RBC tests with TAS of \$35,116 at December 31, 2008, compared to Company Action Level Surplus of \$30,721 at December 31, 2008.

### **10. Employee Benefit Plans**

The Company has a 401(k) defined contribution plan covering substantially all employees. Under the 401(k) plan, the Company matches 50% of employee contributions up to 6% of the employee's salary. Amounts expensed for this plan totaled \$241 and \$240 in 2009 and 2008, respectively.

The Company may make discretionary non-elective 401(k) profit sharing contributions, allocated to all eligible participants in proportion to compensation. In addition, starting January 1, 2007, the Board of Directors authorized the Company to make an age-based non-elective profit sharing contribution, allocated to each participant as a percentage of compensation that equals 4%, 6%, or 8% based on the participant's age under the age-based contribution formula. The Company may make a grandfathered non-elective profit sharing contribution (if greater than the participant's age-based non-elective contribution), allocated to each participant in accordance with the schedule of contributions furnished each year to the Company by the Plan actuary. The grandfather plan calculation is based on the benefit that would accrue under the Company's terminated defined benefit pension plan and is only allocated to employees who were employed before January 1, 2007 and who were at least age 35 by such date. The Company expensed \$25 and \$828 for the years ended December 31, 2009 and 2008, respectively.

The Company has a key-employee long-term performance incentive plan (KELPIP) which allows for incentive compensation for senior management based on growth in surplus and gross written premium over a cumulative three-year measurement cycle. Credits associated with this plan totaled \$0 and \$(417) in 2009 and 2008, respectively. Expenses accrued in 2006 and 2007 were reversed in 2008 based upon operating results and a decline in surplus.

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 10. Employee Benefit Plans (continued)

On June 5, 2007, the Board approved the combined and amended Supplemental Executive Retirement Plan (SERP). The new plan consolidated the original plan dated June 13, 1994 with the amended plan dated November 30, 2005 and made the combined Plan Section 409A compliant. Contributions to the SERP amounted to \$226 in both 2009 and 2008. As of December 31, 2009 and 2008, the Company accrued \$0 and \$1,456, respectively, related to the SERP.

### 11. Commitments and Contingencies

The Company is party to various claims and lawsuits arising in the normal course of business. It is the opinion of management, after consultation with legal counsel, that the disposition of these matters will not have a material adverse effect on the financial position or results of operations of the Company.

Rent expense for all leased properties consisted of the following for the years ended December 31:

	<u>2009</u>	<u>2008</u>
Basic expense	\$ 1,467	\$ 1,507
Sublease income	(427)	(424)
Net rental expense	<u>\$ 1,040</u>	<u>\$ 1,083</u>

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 11. Commitments and Contingencies (continued)

Future minimum lease payments and future minimum lease income at December 31, 2009, under agreements classified as operating leases with noncancelable terms in excess of one year, are as follows:

	<b>Total Obligation</b>	<b>Sublease Income</b>	<b>Net Obligation</b>
2010	\$ 1,384	\$ (256)	\$ 1,128
2011	801	–	801
2012	690	–	690
2013	754	–	754
2014	818	–	818
Thereafter	4,745	–	4,745
	\$ 9,192	\$ (256)	\$ 8,936

The Company entered into a \$1,836 operating lease on June 20, 2008 for internally developed software used for eBusiness. Under terms of the lease, the Company is required to make 36 payments of \$53, plus applicable sales/use tax. In 2009 and 2008, the Company paid \$639 and \$330, respectively.

On March 1, 2009, the Company entered into phase 2 of the eBusiness operating lease with equipment valued at \$871. The term of the lease is 36 months with monthly payments of \$25. In 2009, CAMICO paid 10 payments totaling \$246 under this lease. The proceeds from the lease were invested in a pledged Certificate of Deposit at Comerica and the secured interest in the Certificate of Deposit is periodically released as the principal value of the lease is paid down. Future payments for the two leases are as follows:

	<b>Total Obligation</b>
2010	\$ 934
2011	604
2012	50
	\$ 1,588

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### 11. Commitments and Contingencies (continued)

At the end of the lease, the Company has the opportunity to extend the lease for four months or purchase the equipment at fair value.

### 12. Liability for Unpaid Losses and Loss Adjustment Expenses

Activity in the liability for unpaid losses and LAE, net of reinsurance, is summarized as follows:

	<b>2009</b>	<b>2008</b>
Net balance at January 1	\$ <b>87,733</b>	\$ 76,134
Incurred related to:		
Current year	<b>29,741</b>	43,931
Prior years	<b>292</b>	6,665
Total incurred	<b>30,033</b>	50,596
Paid related to:		
Current year	<b>5,226</b>	6,076
Prior years	<b>35,262</b>	32,921
Total paid	<b>40,488</b>	38,997
Net balance at December 31	<b>\$ 77,278</b>	\$ 87,733

Estimates of incurred losses and LAE attributable to insured events of prior years increased by \$292 in 2009 due to adverse loss and LAE development of \$3,949 for accident years 2005 and prior, partially offset by favorable loss and LAE development of \$3,657 in accident years 2006 through 2008. The adverse development in the 2005 accident year is principally attributable to the late emergence of claims. The favorable development in the 2006 through 2008 accident years is primarily related to the Company's reinsurance agreements and the recessionary impact on incurred losses and LAE being less than anticipated.

Estimates of incurred losses and LAE attributable to insured events of prior years increased by \$6,665 in 2008 due to net adverse Loss and LAE development of \$6,583 in accident years 2005 through 2007, net favorable development of \$82 for accident years 2004 and prior, including adverse development in Adjusting and Other reserves of \$1,095. The adverse development was principally due to increasing IBNR reserves to recognize risks associated with late claim emergence, anticipated increases in claims frequency and severity related to the financial credit crisis, and the Madoff ponzi scheme.

## CAMICO Mutual Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

#### 13. Line of Credit

The Company has a secured revolving line of credit at Prime with Wells Fargo Bank. In November 2008, the line increased to \$10,000 at a rate of prime plus 0.25% with a LIBOR option. On December 15, 2009, the line was reduced to \$5,000 at a rate of prime plus 0.25% with a LIBOR option. The Company maintained pledged bonds with a par value of \$5,800 and money market securities of \$579 at December 31, 2009 as security for the line of credit. There was no balance outstanding on the line of credit at December 31, 2009 and 2008.

#### 14. Nonadmitted Assets

Unassigned surplus decreased by \$1,823 in 2009 and \$3,650 in 2008 as a result of changes in nonadmitted assets. The cumulative affect of the nonadmitted assets along with the change for each year is as follows:

	<b>Cumulative Decrease in Surplus</b>	<b>Current Year Increase (Decrease) in Surplus</b>
<b>December 31, 2009</b>		
Premium receivables over 90 days due	\$ (149)	\$ 57
Nonadmitted deferred tax assets ( <i>Note 6</i> )	(6,764)	(1,814)
EDP equipment and software	(813)	(78)
Furniture, equipment and leasehold improvements	(203)	17
Deposits and prepaids	(611)	(5)
	<b>\$ (8,540)</b>	<b>\$ (1,823)</b>
 <b>December 31, 2008</b>		
Premium receivables over 90 days due	\$ (206)	\$ (89)
Nonadmitted deferred tax assets ( <i>Note 6</i> )	(4,950)	(4,230)
EDP equipment and software	(735)	818
Furniture, equipment and leasehold improvements	(220)	84
Deposits and prepaids	(606)	(233)
	<b>\$ (6,717)</b>	<b>\$ (3,650)</b>

# CAMICO Mutual Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

(Dollars in Thousands)

### **15. Related Party Transactions**

The Company provides certain administrative services related to professional liability policies brokered through CSI, under the terms of a cost sharing agreement. As of December 31, 2009, \$45 was due from the Company to CSI. No intercompany balances were due to or from CSI as of December 31, 2008, as CSI was not conducting business. Net costs allocated from the Company to CSI for the years ended December 31, 2009 and 2008, were \$1,075 and \$0, respectively.

### **16. Subsequent Event**

The Company entered into a casualty excess of loss treaty on new and renewal policies effective January 1, 2010, ceding losses of \$500 excess of \$500 per claim, as the Quota Share Treaty was not renewed. This treaty continues to allow the Company to maintain a writing level that services the CPA community, reduces the net written premium to surplus ratio, and reduces the Company's maximum exposure to \$500 per claim as of January 1, 2010.

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