

Edgar Filing: UNITED FIRE GROUP INC - Form 10-K

UNITED FIRE GROUP INC

Form 10-K

February 28, 2019

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us-gaap:FederalHomeLoanMortgageCorporationFhlmcInsuredLoansMember  
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us-gaap:ShortDurationInsuranceContractsAccidentYear2017Member 2017-12-31 0000101199 ufcs:PersonalMember  
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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-K**

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2018  
OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-34257

**UNITED FIRE GROUP, INC.**

(Exact name of registrant as specified in its charter)

Iowa 45-2302834  
(State or other jurisdiction of incorporation or organization) (I.R.S Employer Identification No.)

118 Second Avenue SE  
Cedar Rapids, Iowa 52401

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (319) 399-5700

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$0.001 par value	The NASDAQ Global Select Market

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES  NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES  NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES  NO

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The aggregate market value of voting stock held by non-affiliates of the registrant as of June 30, 2018 was approximately \$1.1 billion. For purposes of this calculation, all directors and executive officers of the registrant are considered affiliates. As of February 26, 2019, 25,112,309 shares of common stock were outstanding.

### **DOCUMENTS INCORPORATED BY REFERENCE**

Part III of this Form 10-K incorporates by reference certain information from the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A of the Securities Exchange Act of 1934, as amended, for its annual shareholder meeting to be held on May 15, 2019.

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**FORWARD-LOOKING INFORMATION**

This report may contain forward-looking statements about our operations, anticipated performance and other similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor under the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934, as amended (the "Exchange Act"), for forward-looking statements. The forward-looking statements are not historical facts and involve risks and uncertainties that could cause actual results to differ from those expected and/or projected. Such forward-looking statements are based on current expectations, estimates, forecasts and projections about United Fire Group, Inc. ("UFG," the "Registrant," the "Company," "we," "us," or "our"), the industry in which we operate, and beliefs and assumptions made by management. Words such as "expect(s)," "anticipate(s)," "intend(s)," "plan(s)," "believe(s)," "continue(s)," "seek(s)," "estimate(s)," "goal(s)," "target(s)," "forecast(s)," "project(s)," "predict(s)," "should," "could," "may," "will continue," "might," "hope," "can" and other words and terms of similar meaning or expression in connection with a discussion of future operations, financial performance or financial condition, are intended to identify forward-looking statements. See Part I, Item 1A "Risk Factors" of this report for more information concerning factors that could cause actual results to differ materially from those in the forward-looking statements.

Risks and uncertainties that may affect the actual financial condition and results of the Company include but are not limited to the following:

- The frequency and severity of claims, including those related to catastrophe losses and the impact those claims have on our loss reserve adequacy; the occurrence of catastrophic events, including international events, significant severe weather conditions, climate change, acts of terrorism, acts of war and pandemics;
- The adequacy of our reserves for property and casualty insurance losses and loss settlement expenses;
- Geographic concentration risk in our property and casualty insurance business;
- The potential disruption of our operations and reputation due to unauthorized data access, cyber-attacks or cyber-terrorism and other security breaches;
- Developments in general economic conditions, domestic and global financial markets, interest rates and other-than-temporary impairment losses that could affect the performance of our investment portfolio;
- Litigation or regulatory actions that could require us to pay significant damages, fines or penalties or change the way we do business;
- Our ability to effectively underwrite and adequately price insured risks;
- Changes in industry trends, an increase in competition and significant industry developments;
- Lowering of one or more of the financial strength ratings of our operating subsidiaries or our issuer credit ratings and the adverse impact such action may have on our premium writings, policy retention, profitability and liquidity;
  - Governmental actions, policies and regulations, including, but not limited to, domestic health care reform, financial services regulatory reform, corporate governance, new laws or regulations or court decisions interpreting existing laws and regulations or policy provisions; changes in laws, regulations and stock exchange requirements relating to corporate governance and the cost of compliance;
- Our relationship with and the financial strength of our reinsurers; and
- Competitive, legal, regulatory or tax changes that affect the distribution cost or demand for our products through our independent agent/agency distribution network.

These are representative of the risks, uncertainties, and assumptions that could cause actual outcomes and results to differ materially from what is expressed in forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report or as of the date they are made. Except as required under the federal securities laws and the rules and regulations of the Securities and Exchange Commission ("SEC"), we do not have any intention or obligation to update publicly any forward-looking statements, whether as a result of new information, future events, or otherwise.



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**PART I.**

**ITEM 1. BUSINESS**

**GENERAL DESCRIPTION**

United Fire Group, Inc. ("UFG", "United Fire", the "Registrant", the "Company", "we", "us", or "our") and its consolidated subsidiaries and affiliates are engaged in the business of writing property and casualty insurance through a network of independent agencies. Our insurance company subsidiaries are currently licensed as a property and casualty insurer in 46 states, plus the District of Columbia. United Fire & Casualty Company was incorporated in Iowa in January 1946. Our principal executive office is located at 118 Second Avenue SE, Cedar Rapids, Iowa 52401; telephone: 319-399-5700.

United Fire Group, Inc. owns 100 percent of one subsidiary, United Fire & Casualty Company. United Fire & Casualty Company owns 100 percent of seven subsidiaries: (1) Addison Insurance Company; (2) Lafayette Insurance Company; (3) United Fire & Indemnity Company; (4) Mercer Insurance Company; (5) Financial Pacific Insurance Company; (6) UFG Specialty Insurance Company; and (7) United Real Estate Holdings Company, LLC. Mercer Insurance Company owns 100 percent of two subsidiaries: (1) Franklin Insurance Company; and (2) Mercer Insurance Company of New Jersey, Inc. United Fire Lloyds is an affiliate of United Fire & Indemnity Company.

In 2015, the Company dissolved three of its holding companies in order to flatten our organizational chart. The companies dissolved were American Indemnity Financial Corporation, Mercer Insurance Group, Inc. and Financial Pacific Insurance Group, Inc. In addition, Texas General Indemnity Company was renamed to UFG Specialty Insurance Company on July 1, 2015.

**Reportable Segments and Discontinued Operations**

We have historically reported our operations in two business segments: property and casualty insurance and life insurance. On September 18, 2017, the Company signed a definitive agreement to sell its subsidiary, United Life Insurance Company ("United Life"), to Kuvare US Holdings, Inc. ("Kuvare") and on March 30, 2018, the sale closed. As a result, our life insurance business, previously a separate segment, was considered held for sale and reported as discontinued operations in the Consolidated Balance Sheets, Consolidated Statements of Income and Comprehensive Income and Consolidated Statements of Cash Flows (collectively, the "Consolidated Financial Statements").

Subsequent to the announcement of this sale, our continuing operations were reported as one business segment. All current and prior periods reflected in this Form 10-K have been presented as continuing and discontinued operations, unless otherwise noted. For more information, refer to Note 17 "Discontinued Operations" contained in Part II, Item 8, "Financial Statements and Supplementary Data." Additionally, for a detailed discussion of our operating results by continuing operations and discontinued operations, refer to the "Consolidated Results of Operations" section in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Our property and casualty insurance business is comprised of commercial lines insurance, including surety bonds, personal lines insurance and assumed reinsurance. All of our property and casualty insurance subsidiaries and our affiliate belong to an intercompany reinsurance pooling arrangement. On July 1, 2015, UFG Specialty Insurance Company entered the pooling arrangement. Pooling arrangements permit the participating companies to rely on the capacity of the entire pool's capital and surplus, rather than being limited to policy exposures of a size commensurate with each participant's own surplus level. Under such arrangements, the members share substantially all of the insurance business that is written and allocate the combined premiums, losses and expenses based on percentages defined in the arrangement.

**Employees**

As of December 31, 2018, we employed 1,160 full-time employees and 23 part-time employees. We are not a party to any collective bargaining agreement.

**Available Information**

We provide free and timely access to all our reports filed with the SEC in the Investor Relations section of our website at [www.ufginsurance.com](http://www.ufginsurance.com). Under the "Investors" tab, select "Financial Documents" and then, select "SEC Filings" to view the list of our SEC filings, which includes annual reports on Form 10-K, quarterly reports on Form



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10-Q, current reports on Form 8-K, proxy statements, beneficial ownership reports on Forms 3, 4 and 5 and amendments to reports filed or furnished pursuant to Section 13(a), 15(d) or 16(a) of the Exchange Act. Such reports are made available as soon as reasonably practicable after they are filed with or furnished to the SEC. They are also available on the SEC's website at [www.sec.gov](http://www.sec.gov).

Our Code of Ethics and Business Conduct is also available at [www.ufginsurance.com](http://www.ufginsurance.com) in the Investor Relations section. To view it, under the "Investors" tab, select "Governance Documents" and then "Code of Ethics and Business Conduct."

Free paper copies of any materials that we file with or furnish to the SEC can also be obtained by writing to Investor Relations, United Fire Group, Inc., 118 Second Avenue SE, Cedar Rapids, Iowa 52401.

**MARKETING AND DISTRIBUTION**

We market our products through our home office in Cedar Rapids, Iowa, and five regional offices: (1) Westminster, Colorado, a suburb of Denver; (2) Webster, Texas, a suburb of Houston; (3) Pennington, New Jersey; (4) Phoenix, Arizona; and (5) Rocklin, California. We are represented through approximately 1,100 independent property and casualty agencies.

**Continuing Operations - Property and Casualty Insurance Business**

We staff our regional offices with underwriting, claims and marketing representatives and administrative technicians, all of whom provide support and assistance to the independent agencies. Also, home office staff technicians and specialists provide support to our subsidiaries, regional offices and independent agencies. We use management reports to monitor subsidiary and regional offices for overall results and conformity to our business policies.

**Competition**

The property and casualty insurance industry is highly competitive. We compete with numerous property and casualty insurance companies in the regional and national market, many of which are substantially larger and have considerably greater financial and other resources. Except for regulatory considerations, there are limited barriers to entry into the insurance industry. Our competitors may be domestic or foreign, as well as licensed or unlicensed. The exact number of competitors within the industry is not known. Insurers compete on the basis of reliability, financial strength and stability, ratings, underwriting consistency, service, business ethics, price, performance, capacity, policy terms and coverage conditions.

In addition, because our products are marketed exclusively through independent insurance agencies, most of which represent more than one company, we face competition within each agency and competition to retain qualified independent agents. Our competitors include companies that market their products through agents, as well as companies that sell insurance directly to their customers.

Because we rely solely on independent agencies, we offer a competitive commissions program and a rewarding profit-sharing plan as incentives for agents to place high-quality property and casualty insurance business with us. Property and casualty insurance agencies will receive profit-sharing payments of \$21.4 million in 2019, based on profitable business produced by the agencies in 2018. In 2018 for 2017 business, agencies received \$15.1 million in profit-sharing payments and in 2017 for 2016 business, agencies received \$16.1 million in payments.

Our competitive advantages include our commitment to:

**Strong agency relationships** —

A stable workforce, with an average duration of employment of approximately 9.1 years, allows our agents to work with the same, highly-experienced personnel each day.

Our organization is relatively flat, allowing our agents to be close to the highest levels of management and ensuring that our agents will receive answers quickly to their questions.

**Exceptional service** — our agents and policyholders always have the option to speak with a real person.

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• Fair and prompt claims handling — we view claims as an opportunity to prove to our customers that they have chosen the right insurance company.

• Disciplined underwriting — we empower our underwriters with the knowledge and tools needed to make good decisions for the Company.

• Superior loss control services — our loss control representatives make multiple visits to businesses and job sites each year to ensure safety.

• Effective and efficient use of technology — we use technology to provide enhanced service to our agents and policyholders, not to replace our personal relationships, but to reinforce them.

**Discontinued Operations - Life Insurance Business**

Our life insurance subsidiary marketed its products primarily in the Midwest, East Coast and West.

**REINSURANCE**

Incorporated by reference from Note 4 "Reinsurance" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**RESERVES**

**Continuing Operations - Property and Casualty Insurance Business**

Property insurance indemnifies an insured with an interest in physical property for loss of, or damage to, such property or the loss of its income-producing abilities. Casualty insurance primarily covers liability for damage to property of, or injury to, a person or entity other than the insured. In most cases, casualty insurance also obligates the insurance company to provide a defense for the insured in litigation, arising out of events covered by the policy. Liabilities for loss and loss settlement expenses reflect management's best estimates at a given point in time of what we expect to pay for claims that have been reported and those that have been incurred but not reported ("IBNR"), based on known facts, circumstances, and historical trends.

The determination of reserves (particularly those relating to liability lines of insurance that have relatively longer lag in claim reporting) requires significant work to reasonably project expected future claim reporting and payment patterns. If, during the course of our regular monitoring of reserves, we determine that coverages previously written are incurring higher than expected losses, we will take action that may include, among other things, increasing the related reserves. Any adjustments we make to reserves are reflected in operating results in the year in which we make those adjustments. We engage an independent actuary, Regnier Consulting Group, Inc. ("Regnier"), to render an opinion as to the reasonableness of our statutory reserves annually. The actuarial opinion is filed in those states where we are licensed.

On a quarterly basis, United Fire's internal actuary performs a detailed actuarial review of IBNR reserves. This review includes a comparison of results from the most recent analysis of reserves completed by both our internal and external actuaries. Senior management meets with our internal actuary to review, on a quarterly basis, the adequacy of carried reserves based on results from this actuarial analysis. There are two fundamental types or sources of IBNR reserves. We record IBNR reserves for "normal" types of claims and also specific IBNR reserves related to unique circumstances or events. A major hurricane is an example of an event that might necessitate establishing specific IBNR reserves because an analysis of existing historical data would not provide an appropriate estimate.

We do not discount loss reserves based on the time value of money.

For a more detailed discussion of our loss reserves, refer to the "Critical Accounting Policies" section in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 5 "Reserves for Losses and Loss Settlement Expenses" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**Discontinued Operations - Life Insurance Business**

Prior to the sale of our life insurance business, we calculated the policy reserves in accordance with U.S generally accepted accounting principles ("GAAP"). In the Consolidated Balance Sheets, these reserves are presented in prior

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periods in Liabilities held for sale. For our fixed annuities and universal life policies, we established a benefit reserve at the time of policy issuance in an amount equal to the deposits received. Subsequently, we adjusted the benefit reserve for any additional deposits, interest credited and partial or complete withdrawals, as well as insurance and other expense charges. We based policy reserves for other life products on the projected contractual benefits and expenses and interest rates appropriate to those products. We based reserves for accident and health products, which are a minor portion of our reserves, on appropriate morbidity tables.

We determined reserves for statutory purposes based upon mortality rates and interest rates specified by Iowa state law. Our life insurance subsidiary's reserves met or exceeded the minimum statutory requirements. Griffith, Ballard & Company, an independent actuary, assisted us in developing and analyzing our reserves on both a GAAP and statutory basis.

For further discussion of our life insurance reserves, refer to the "Critical Accounting Policies" section in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

**INVESTMENTS**

Incorporated by reference from Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," under the headings "Investments," "Market Risk" and "Critical Accounting Policies"; and Note 1 "Significant Accounting Policies" under the headings "Investments," Note 2 "Summary of Investments," and Note 3 "Fair Value of Financial Instruments," contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**REGULATION**

The insurance industry is subject to comprehensive and detailed regulation and supervision. Each jurisdiction in which we operate has established supervisory agencies with broad administrative powers. While we are not aware of any currently proposed or recently enacted state or federal regulation that would have a material impact on our operations, we cannot predict the effect that future regulatory changes might have on us.

**State Regulation**

We are subject to extensive regulation, primarily at the state level. The method, extent and substance of such regulation varies by state, but generally has its source in National Association of Insurance Commissioners ("NAIC") model laws and regulations that establish standards and requirements for conducting the business of insurance and that delegate regulatory authority to a state regulatory agency. Moreover, the NAIC Accreditation Program requires state regulatory agencies to meet baseline standards of solvency regulation, particularly with respect to regulation of multi-state insurers. In general, such regulation is intended for the protection of those who purchase or use our insurance products, and not our shareholders. These rules have a substantial effect on our business and relate to a wide variety of matters including: insurance company licensing and examination; the licensing of insurance agents and adjusters; price setting or premium rates; trade practices; approval of policy forms; claims practices; restrictions on transactions between our subsidiaries and their affiliates, including the payment of dividends; investments; underwriting standards; advertising and marketing practices; capital adequacy; and the collection, remittance and reporting of certain taxes, licenses and fees.

The state laws and regulations that have the most significant effect on our insurance operations and financial reporting are discussed below.

***Insurance Holding Company Regulation***

We are regulated as an insurance holding company system in the states of domicile of our property and casualty insurance companies: Iowa (United Fire & Casualty Company, UFG Specialty Insurance Company and Addison Insurance Company), California (Financial Pacific Insurance Company), Louisiana (Lafayette Insurance Company), New Jersey (Mercer Insurance Company of New Jersey, Inc.), Pennsylvania (Mercer Insurance Company and Franklin Insurance Company) and Texas (United Fire & Indemnity Company and United Fire Lloyds). These regulations require that we annually furnish financial and other information about the operations of the individual companies within our holding company system. Generally, the insurance laws of these states provide that notice to the state insurance commissioner is required before finalizing any transaction affecting the ownership or control of an insurer and before finalizing certain material transactions between an insurer and any person or entity within its



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holding company system. In addition, some of those transactions cannot be finalized without the commissioner's prior approval.

Most states have now adopted the version of the Model Insurance Holding Company System Regulation Act and Regulation as amended by the NAIC in December 2010 (the "Amended Model Act") to introduce the concept of "enterprise risk" within an insurance company holding system. Enterprise risk is defined as any activity, circumstance, event or series of events involving one or more affiliates of an insurer that, if not remedied promptly, is likely to have a material adverse effect upon the financial condition or the liquidity of the insurer or its insurance holding company system as a whole. The Amended Model Act imposes more extensive informational requirements on us, including requiring us to prepare an annual enterprise risk report that identifies the material risks within our insurance company holding system that could pose enterprise risk to our licensed insurers. Compliance with new reporting requirements under the Amended Model Act began for us in 2014 for the 2013 fiscal year.

***Restrictions on Shareholder Dividends***

As an insurance holding company with no independent operations or source of revenue, our capacity to pay dividends to our shareholders is based on the ability of our insurance company subsidiaries to pay dividends to us. The ability of our subsidiaries to pay dividends to us is regulated by the laws of their state of domicile. Under these laws, insurance companies must provide advance informational notice to the domicile state insurance regulatory authority prior to payment of any dividend or distribution to its shareholders. Prior approval from the state insurance regulatory authority must be obtained before payment of an "extraordinary dividend" as defined under the state's insurance code. The amount of ordinary dividends that may be paid to us is subject to certain limitations, the amounts of which change each year. In all cases, we may pay dividends only from our earned surplus. Refer to the "Market Information" section of Part II, Item 5, "Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities," and Note 6 "Statutory Reporting, Capital Requirements and Dividends and Retained Earnings Restrictions," contained in Part II, Item 8, "Financial Statements and Supplementary Data" for additional information about the dividends we paid during 2018.

***Price Regulation***

Nearly all states have insurance laws requiring us to file rate schedules, policy or coverage forms, and other information with the state's regulatory authority. In certain states, rate schedules, policy forms, or both, must be approved prior to use. While insurance laws vary from state to state, their objectives are generally the same: an insurance rate cannot be excessive, inadequate or unfairly discriminatory. The speed with which we can change our rates in response to competition or in response to increasing costs depends, in part, on the willingness of state regulators to allow adequate rates for the business we write.

***Investment Regulation***

We are subject to various state regulations requiring investment portfolio diversification and limiting the concentration of investments we may maintain in certain asset categories. Failure to comply with these regulations leads to the treatment of nonconforming investments as nonadmitted assets for purposes of measuring statutory surplus. Further, in some instances, state regulations require us to sell certain nonconforming investments.

***Exiting Geographic Markets; Canceling and Nonrenewing Policies***

Most states regulate our ability to exit a market. For example, states limit, to varying degrees, our ability to cancel and non-renew insurance policies. Some states prohibit us from withdrawing one or more types of insurance business from the state, except upon prior regulatory approval. Regulations that limit policy cancellation and non-renewal may restrict our ability to exit unprofitable markets.

***Insurance Guaranty Associations***

Each state has insurance guaranty association laws. Membership in a state's insurance guaranty association is generally mandatory for insurers wishing to do business in that state. Under these laws, associations may assess their members for certain obligations that insolvent insurance companies have incurred with regard to their policyholders and claimants.

Typically, states assess each solvent association member with an amount related to that member's proportionate share of business written by all association members within the state. Most state guaranty associations allow solvent





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insurers to recoup the assessments they are charged through future rate increases, surcharges or premium tax credits. However, there is no assurance that we will ultimately recover these assessments. We cannot predict the amount and timing of any future assessments or refunds under these laws.

***Shared Market and Joint Underwriting Plans***

State insurance regulations often require insurers to participate in assigned risk plans, reinsurance facilities and joint underwriting associations. These are mechanisms that generally provide applicants with various types of basic insurance coverage that may not otherwise be available to them through voluntary markets. Such mechanisms are most commonly instituted for automobile and workers' compensation insurance, but many states also mandate participation in Fair Access to Insurance Requirements ("FAIR") Plans or Windstorm Plans, which provide basic property coverage. Participation is based upon the amount of a company's voluntary market share in a particular state for the classes of insurance involved. Policies written through these mechanisms may require different underwriting standards and may pose greater risk than those written through our voluntary application process.

***Statutory Accounting Rules***

For public reporting, insurance companies prepare financial statements in accordance with GAAP. However, state laws require us to calculate and report certain data according to statutory accounting rules as defined in the NAIC Accounting Practices and Procedures Manual. While not a substitute for any GAAP measure of performance, statutory data frequently is used by industry analysts and other recognized reporting sources to facilitate comparisons of the performance of insurance companies.

***Insurance Reserves***

State insurance laws require that insurance companies analyze the adequacy of their reserves annually. Our appointed actuaries must submit an opinion that our statutory reserves are adequate to meet policy claims-paying obligations and related expenses.

***Financial Solvency Ratios***

The NAIC annually calculates 13 financial ratios to assist state insurance regulators in monitoring the financial condition of insurance companies. A "usual range" of results for each of these ratios is used by insurance regulators as a benchmark. Departure from the usual range on four or more of the ratios could lead to inquiries from individual state insurance departments as to certain aspects of a company's business. In addition to the financial ratios, states also require us to calculate a minimum capital requirement for each of our insurance companies based on individual company insurance risk factors. These "risk-based capital" results are used by state insurance regulators to identify companies that require regulatory attention or the initiation of regulatory action. At December 31, 2018, all of our insurance companies had capital in excess of the required levels.

***Federal Regulation***

Although the federal government and its regulatory agencies generally do not directly regulate the business of insurance, federal initiatives and legislation often have an impact on our business. These initiatives and legislation include tort reform proposals, proposals addressing natural catastrophe exposures, terrorism risk mechanisms, federal financial services reforms, various tax proposals affecting insurance companies, and possible regulatory limitations, impositions and restrictions arising from the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), and the Patient Protection and Affordable Care Act.

Various legislative and regulatory efforts to reform the tort liability system have impacted and will continue to impact our industry. Although there has been some tort reform with positive impact to the insurance industry, new causes of action and theories of damages continue to be proposed in state court actions or by federal or state legislatures that continue to expand liability for insurers and their policyholders. For example, some state legislatures have from time-to-time considered legislation addressing direct actions against insurers related to bad faith claims. As a result of this unpredictability in the law, insurance underwriting is expected to continue to be difficult in commercial lines, professional liability and other specialty coverages.

Dodd-Frank expanded the federal presence in insurance oversight and may increase regulatory requirements that are applicable to us. Dodd-Frank's requirements include streamlining the state-based regulation of reinsurance and non-admitted insurance (property or casualty insurance placed with insurers that are eligible to accept insurance, but are



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not licensed to write insurance in a particular state). Dodd-Frank also established the Federal Insurance Office within the U.S. Department of the Treasury that is authorized to, among other things, gather data and information to monitor aspects of the insurance industry, identify issues in the regulation of insurers about insurance matters, and preempt state insurance measures under certain circumstances.

Dodd-Frank also contains a number of provisions related to corporate governance and disclosure matters. In response to Dodd-Frank, the SEC has adopted or proposed rules regarding director independence, director and officer hedging activities, executive compensation clawback policies, compensation advisor independence, pay versus performance disclosures, internal pay equity disclosures, and shareholder proxy access. We continue to monitor developments under Dodd-Frank and their impact on us, insurers of similar size and the insurance industry as a whole.

The Patient Protection and Affordable Care Act and the related amendments in the Health Care and Education Reconciliation Act may increase our operating costs and underwriting losses. This landmark legislation continues to result in numerous changes within the health care industry that could create additional operating costs for us, particularly with respect to our workers' compensation products.

**FINANCIAL STRENGTH AND ISSUER CREDIT RATING**

Our financial strength, as measured by statutory accounting principles, is regularly reviewed by an independent rating agency that assigns a rating based upon criteria such as results of operations, capital resources and minimum policyholders' surplus requirements. An insurer's financial strength rating is one of the primary factors evaluated by those in the market to purchase insurance. A poor rating indicates that there is an increased likelihood that the insurer could become insolvent and therefore not able to fulfill its obligations under the insurance policies it issues. This rating can also affect an insurer's level of premium writings, the lines of business it can write and, for insurers like us that are also public registrants, the market value of its securities.

Our property and casualty insurers are rated by A.M. Best Company ("A.M. Best") on a group basis. Our pooled property and casualty insurers have all received an "A" (Excellent) financial strength rating from A.M. Best. . According to A.M. Best, companies rated "A" have "an excellent ability to meet their ongoing obligations to policyholders."

A.M. Best also assigns issuer credit ratings based on a company's ability to repay its debts. All of our property and casualty insurers have received an issuer credit rating of "a" from A.M. Best. Beginning in 2012, our holding company parent was also rated by A.M. Best, receiving an issuer credit rating of "bbb."

**EXECUTIVE OFFICERS OF THE COMPANY**

The following table sets forth information concerning the following executive officers:

<b>Name</b>	<b>Age</b>	<b>Position</b>
Randy A. Ramlo	57	President and Chief Executive Officer
Michael T. Wilkins	55	Executive Vice President and Chief Operating Officer
Dawn M. Jaffray	52	Senior Vice President and Chief Financial Officer
Barrie W. Ernst	64	Vice President and Chief Investment Officer
Neal R. Scharmer	62	Vice President, General Counsel and Corporate Secretary

A brief description of the business experience of these officers follows:

Randy A. Ramlo became our President and Chief Executive Officer in May 2007. He previously served as our Chief Operating Officer from May 2006 until May 2007, as Executive Vice President from May 2004 until May 2007, and as Vice President, Fidelity and Surety, from November 2001 until May 2004. He also worked as an underwriting manager in our Great Lakes region. Mr. Ramlo began his employment with us as an underwriter in 1984.

Michael T. Wilkins became our Executive Vice President and Chief Operating Officer in May 2014. He served as our Executive Vice President, Corporate Administration, from May 2007 to May 2014. He was our Senior Vice President, Corporate Administration, from May 2004 until May 2007, our Vice President, Corporate Administration,

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from August 2002 until May 2004 and the resident Vice President in our Lincoln regional office from 1998 until 2002. Prior to 1998, Mr. Wilkins held various other positions within the Company since joining us in 1985.

Dawn M. Jaffray became our Senior Vice President and Chief Financial Officer in May 2015. Ms. Jaffray previously served as Chief Financial Officer of Soleil Advisory Group, a consulting firm specializing in operational consulting, mergers and acquisitions, investment and strategy from 2009 to 2015. Prior to her service with Soleil Advisory Group, Ms. Jaffray held numerous positions in insurance operations and mergers/acquisition activities, primarily in the role of principal financial officer. Ms. Jaffray's business experience has been focused in particular on insurance, finance and capital management.

Barrie W. Ernst is our Vice President and Chief Investment Officer. He joined us in August 2002. Previously, Mr. Ernst served as Senior Vice President of SCI Financial Group in Cedar Rapids, Iowa, where he worked from 1980 to 2002. SCI Financial Group was a regional financial services firm providing brokerage, insurance and related services to its clients.

Neal R. Scharmer was appointed our Vice President and General Counsel in May 2001 and Corporate Secretary in May 2006. He joined us in 1995.

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**ITEM 1A. RISK FACTORS**

We provide readers with the following discussion of risks and uncertainties relevant to our business. These are factors that we believe could cause our actual results to differ materially from our historic or anticipated results. We could also be adversely affected by other factors, in addition to those listed here. Additional information concerning factors that could cause actual results to differ materially from those contained in the forward-looking statements is set forth in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Risks Relating to Our Business**

*The occurrence, frequency and severity of catastrophe losses are unpredictable and may adversely affect our results of operations, liquidity and financial condition.*

Our property and casualty insurance operations expose us to claims arising from catastrophic events affecting multiple policyholders. Such catastrophic events consist of various natural disasters, including, but not limited to, hurricanes, tornadoes, windstorms, hailstorms, fires and wildfires, earthquakes, severe winter weather, tropical storms, volcanic eruptions and man-made disasters such as terrorist acts (including biological, chemical or radiological events), explosions, infrastructure failures and results from political instability. We have exposure to tropical storms and hurricanes along the Gulf Coast, Eastern and Southeastern coasts of the United States. We have exposure to tornadoes, windstorms and hail storms throughout the United States. We have exposure to earthquakes along the West Coast and the New Madrid Fault area. Our automobile and inland marine business also exposes us to losses arising from floods and other perils.

Property damage resulting from catastrophes is the greatest risk of loss we face in the ordinary course of our business. We have exposure to catastrophe losses under both our commercial insurance policies and our personal insurance policies. The losses from catastrophic events are a function of both the extent of our exposure, the frequency and severity of the events themselves and the level of reinsurance assumed and ceded. For example, the losses experienced from a tornado will vary on whether the location of the tornado was in a highly populated or unpopulated area, the concentration of insureds in that area and the severity of the tornado. Increases in the value and geographic concentration of insured property and the effects of inflation could increase the severity of claims from a catastrophic event.

Long-term weather trends may be changing and new types of catastrophe losses may be developing due to climate change, which is a phenomenon that has been associated with extreme weather events linked to rising temperatures, including effects on global weather patterns, greenhouse gases, sea, land and air temperature, sea levels, rain and snow. While the emerging science regarding climate change and its connection to extreme weather events continues to be debated, in recent years there has been an increase in frequency and severity of tornadoes and hailstorms, and hurricanes are now impacting areas further inland than experienced in the recent past. Such changes in climate conditions could cause our underlying modeling data to be less accurate, limiting our ability to evaluate and manage our risk.

In addition, as with catastrophe losses generally, it can take a long time for us to determine our ultimate losses associated with a particular catastrophic event. The inability to access portions of the impacted area, the complexity of the losses, legal and regulatory uncertainty and the nature of the information available for certain catastrophic events may affect our ability to estimate the claims and claim adjustment expense reserves. Such complex factors include, but are not limited to: determining the cause of the damage, evaluating general liability exposures, estimating additional living expenses, the impact of demand surge, infrastructure disruption, fraud, business interruption costs and reinsurance collectability.

The timing of a catastrophic occurrence at the end or near the end of a reporting period may also affect the information available to us when estimating claims and claim adjustment expense reserves for the reporting period. As our claims experience for a particular catastrophe develops, we may be required to adjust our reserves to reflect our revised estimates of the total cost of claims. However, because the occurrence and severity of catastrophes are inherently unpredictable and may vary significantly from year to year and region to region, historical results of operations may not be indicative of future results of operations.



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Catastrophes may reduce our net income, cause substantial volatility in our financial results for any fiscal quarter or year or otherwise adversely affect our financial condition, liquidity or results of operations. Catastrophes may also negatively affect our ability to write new business.

Following catastrophes there are also sometimes legislative, administrative and judicial decisions that seek to expand insurance coverage for claims beyond the original intent of the policies or seek to prevent the application of deductibles. Our ability to manage catastrophic exposure may be limited by public policy considerations, the political environment, changes in the general economic climate and/or social responsibilities.

***Our reserves for property and casualty insurance losses and loss settlement expenses are based on estimates and may be inadequate, adversely impacting our financial results.***

We maintain insurance reserves to cover our estimated ultimate unpaid liability for claim and claim adjustment expenses, including the estimated cost of the claims adjustment process, for reported and unreported claims and for future policy benefits. Our reserves may prove to be inadequate, which may result in future charges to earnings and/or a downgrade of our financial strength rating or the financial strength ratings of our insurance company subsidiaries. Insurance reserves represent our best estimate at a given point in time. They are not an exact calculation of liability but instead are complex estimates, which are a product of actuarial expertise and projection techniques from a number of assumptions and expectations about future events, many of which are highly uncertain.

The process of estimating claims and claims adjustment expense reserves involves a high degree of judgment. These estimates are based on historical data and the impact of various factors such as:

- actuarial and statistical projections of the cost of settlement and administration of claims reflecting facts and circumstances then known;
- historical claims information and loss emergence patterns;
- assessments of currently available data;
- estimates of future trends in claims severity and frequency;
- judicial theories of liability;
- economic factors such as inflation;
- estimates and assumptions regarding social, judicial and legislative trends, and actions such as class action lawsuits and judicial interpretation of coverages or policy exclusions; and
- the level of insurance fraud.

Many of these factors are not quantifiable. The inherent uncertainties of estimating reserves are greater for certain types of liabilities, particularly those in which the various considerations affecting the type of claim are subject to change and in which long periods of time may elapse before a definitive determination of liability is made. Reserve estimates are continually refined in a regular and ongoing process as experience develops and further claims are reported and settled.

Along with other insurers, we use internal and external models in assessing our exposure to catastrophe losses that assume various conditions and probability scenarios; however, these models do not necessarily accurately predict future losses or accurately measure losses currently incurred. Models for catastrophes use historical information about various catastrophes and details about our in-force business. While we use this information in our pricing and risk managements, there are limitations with respect to their usefulness in predicting losses in any reporting period. Such limitations lead to questionable predictive capability and post-event measurements that have not been well understood or proven to be sufficiently reliable. In addition, the models are not necessarily reflective of our state-specific policy language, demand surge for labor and materials or loss settlement expenses, all of which are subject to wide variation. Actual loss and loss settlement expenses paid might exceed our reserves. If our loss reserves are insufficient, or if we believe our loss reserves are insufficient to cover our actual loss and loss settlement expenses, we will have to increase our loss reserves and incur charges to our earnings, which could indicate that premium levels were

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insufficient. As such, deviations from one or more of these assumptions could result in a material adverse impact on our Consolidated Financial Statements and our financial strength rating or the financial strength ratings of our insurance company subsidiaries could be downgraded.

For a detailed discussion of our reserving process and the factors we consider in estimating reserves, refer to the "Critical Accounting Policies" section in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

***Our geographic concentration ties our performance to the business, economic and regulatory conditions of certain states.***

The following states provided 48.9 percent of the direct statutory premiums written for the property and casualty insurance businesses in 2018: Texas (17.4 percent), California (11.2 percent), Iowa (8.8 percent), Missouri (6.4 percent) and Colorado (5.1 percent).

Our revenues and profitability are subject to the prevailing regulatory, legal, economic, political, demographic, competitive, weather and other conditions in the principal states in which we do business. With respect to regulatory conditions, the NAIC and state legislators continually reexamine existing laws and regulations, specifically focusing on modifications to holding company regulations, interpretations of existing laws and the development of new laws and regulations. In a time of financial uncertainty or a prolonged economic downturn, regulators may choose to adopt more restrictive insurance laws and regulations. Changes in regulatory or any other of these conditions could make it less attractive for us to do business in such states and would have a more pronounced effect on us compared to companies that are more geographically diversified. In addition, our exposure to severe losses from localized natural perils, such as hurricanes or hailstorms, is increased in those areas where we have written a significant amount of property insurance policies.

***Unauthorized data access, cyber attacks and other security breaches could have an adverse impact on our business and reputation.***

We rely on computer systems to conduct our business for our customer service, marketing and sales activities, customer relationship management and producing financial statements. Our business and operations rely on secure and efficient processing, storage and transmission of customer and Company data, including personally identifiable information. Our ability to effectively operate our business depends upon our ability, and the ability of certain third party vendors and business partners, to access our computer systems to perform necessary business functions, such as providing quotes and product pricing, billing and processing premiums, administering claims, and reporting our financial results.

We retain confidential information on our computer systems, including customer information and proprietary business information belonging to us and our policyholders. Our business and operations depend upon our ability to safeguard this personally identifiable information. Our systems may be vulnerable to unauthorized access and hackers, computer viruses, and other scenarios in which our data may be compromised.

Cyber attacks involving these systems, or those of our third party vendors, could be carried out remotely and from multiple sources and could interrupt, damage, or otherwise adversely affect the operations of these critical systems. Cyber attacks could result in the modification or theft of data, the distribution of false information, or the denial of service to users. Threats to data security can emerge from a variety of sources and change rapidly, resulting in the ongoing need to expend resources to secure our data in accordance with customer expectations and statutory and regulatory requirements.

Any compromise of the security of our data could expose us to liability and harm our reputation, which could affect our business and results of operations. We continually enhance our operating procedures and internal controls to effectively support our business and comply with our regulatory and financial reporting requirements, but there can be no assurances that we will be able to implement security measures adequate to prevent every security breach.

Although, to date, we do not believe we have experienced any material cyber attacks, the occurrence, scope and effect of any cyber attack may remain undetected for a period of time. We maintain cyber liability insurance coverage that provides both third-party liability and first-party insurance coverages; however, our insurance may be insufficient to cover all losses and expenses related to a cyber attack.





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Federal and state policymakers have, and will likely continue to propose increased regulation of the protection of personally identifiable information and appropriate protocols after a related cybersecurity breach. The New York Department of Financial Services recently adopted a cyber protection and reporting regulation for financial services companies with which we are complying. The NAIC has created the Data Security Model Law ("DSML") based upon the New York regulation. We expect several states to adopt the DSML. Compliance with these regulations and efforts to address continually developing cybersecurity risks may result in a material adverse effect on our results of operations, liquidity, financial condition, and financial strength.

***Conditions in the global capital markets and the economy generally may weaken materially and adversely affect our business and results of operations.***

Our results of operations, financial position and liquidity are materially affected by conditions in the global capital markets and the economy generally, both in the U.S. and elsewhere around the world. As a result of such conditions, our policyholders may choose to defer paying insurance premiums or stop paying insurance premiums altogether. In addition, we may experience an elevated incidence of claims and lapses or surrenders of policies causing a change in our exposure.

Factors such as consumer spending, business investment, government spending, the volatility and strength of the capital markets, investor and consumer confidence and inflation levels all affect the business and economic environment and, ultimately, the amount and profitability of our business. In an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment, negative investor sentiment and lower consumer spending, the demand for our insurance products could be adversely affected.

***The effects of emerging claim and coverage issues and class action litigation on our business are uncertain.***

We are subject to certain effects of emerging or potential claims and coverage issues that arise as industry practices and legal, judicial, social, economic and other environmental conditions change, including unexpected and unintended issues related to claims and coverage. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number and/or size of claims, resulting in further increases in our reserves. The effects of these and other unforeseen emerging claim and coverage issues are extremely hard to predict. Examples of these issues include:

- judicial expansion of policy coverage and the impact of new theories of liability;
- an increase of plaintiffs targeting property and casualty insurers, including us, in purported class action litigation regarding claims handling and other practices;
- medical developments that link health issues to particular causes, resulting in liability or workers' compensation (for example, cumulative trauma);
- claims relating to unanticipated consequences of current or new technologies;
- an increase in the variety, number and size of claims relating to liability losses, which often present complex coverage and damage valuation questions;
- claims relating to potentially changing climate conditions, including higher frequency and severity of weather-related events; and
- adverse changes in loss cost trends, including inflationary pressure in medical cost and auto and home repair costs.

***We are subject to certain risks related to our investment portfolio that could negatively affect our profitability.***

Investment income is an important component of our net income and overall profitability. We invest premiums received from policyholders and other available cash to generate investment income and capital appreciation, while also maintaining sufficient liquidity to pay covered claims, operating expenses and dividends. As discussed in detail below, general economic conditions, changes in financial markets and many other factors beyond our control can adversely affect the value of our investments and the realization of investment income.

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We primarily manage our investment portfolio internally under required statutory guidelines and investment guidelines approved by our Board of Directors and the boards of directors of our subsidiaries. Although these guidelines stress diversification and capital preservation, our investments are subject to a variety of risks, including:

*Credit Risk* - The value of our investment in marketable securities is subject to impairment as a result of deterioration in the creditworthiness of the issuer. Such impairments could reduce our net investment income and result in realized investment losses. The vast majority of our investments (99.6% at December 31, 2018) are made in investment-grade securities. Although we try to manage this risk by diversifying our portfolio and emphasizing credit quality, our investments are subject to losses as a result of a general downturn in the economy.

*Interest Rate Risk* - A significant portion of our investment portfolio (85.0 percent at December 31, 2018) consists of fixed income securities, primarily corporate and municipal bonds (75.5 percent at December 31, 2018). These securities are sensitive to changes in interest rates. An increase in interest rates typically reduces the fair value of fixed income securities, while a decline in interest rates reduces the investment income earned from future investments in fixed income securities. In recent periods, interest rates have been at or near historic lows. It is possible that this trend may continue for a prolonged period of time. We generally hold our fixed income securities to maturity, so our interest rate exposure does not usually result in realized losses. However, rising interest rates could result in a significant reduction of the book value of our fixed maturity investments. Low interest rates, and low investable yields, could adversely impact our net earnings as reinvested funds produce lower investment income.

Interest rates are highly sensitive to many factors beyond our control including general economic conditions, changes in governmental regulations and monetary policy, and national and international political conditions.

*Liquidity Risk* - We seek to match the maturities of our investment portfolio with the estimated payment date of our loss and loss adjustment expense reserves to ensure strong liquidity and avoid having to liquidate securities to fund claims. Risk such as inadequate loss and loss adjustment reserves or unfavorable trends in litigation could potentially result in the need to sell investments to fund these liabilities. This could result in significant realized losses depending on the conditions of the general market, interest rates and credit profile of individual securities.

Further, our investment portfolio is subject to increased valuation uncertainties when investment markets are illiquid. The valuation of investments is more subjective when markets are illiquid, thereby increasing the risk that the estimated fair value (i.e., the carrying amount) of the portion of the investment portfolio that is carried at fair value as reflected in our financial statements is not reflective of prices at which actual transactions could occur.

*Market Risk* - Our investments are subject to risks inherent in the global financial system and capital markets. The value and risks of our investments may be adversely affected if the functioning of those markets is disrupted or otherwise affected by local, national or international events, such as: changes in regulation or tax policy; changes in legislation relating to bankruptcy or other proceedings; infrastructure failures; wars or terrorist attacks; the overall health of global economies; a significant change in inflation expectations; a significant devaluation of government or private sector credit and/or currency values; and other factors or events not specifically attributable to changes in interest rates, credit losses, and liquidity needs.

*Credit Spread Risk* - Our exposure to credit spreads primarily relates to market price variability and reinvestment risk associated with changes in credit spreads. Valuations may include assumptions or estimates that may have significant period-to-period changes from market volatility, which could have a material adverse effect on our results of operations or financial condition.

Our fixed maturity investment portfolio is invested substantially in state, municipal and political subdivision bonds.

Our fixed maturity investment portfolio could be subject to default or impairment, in particular:

States and local governments have been operating under deficits or projected deficits which may have an impact on the valuation of our municipal bond portfolio.

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There is a risk of widespread defaults which may increase if some issuers chose to voluntarily default instead of implementing fiscal measures such as increasing tax rates or reducing spending. Such risk may also increase if there are changes in legislation permitting states, municipalities and political subdivisions to file for bankruptcy protection where they were not permitted to before. Judicial interpretations in such bankruptcy proceedings may also adversely affect the collectability of principal and interest, and/or valuation of our bonds. Changes in tax laws impacting marginal tax rates, exemptions, deductions, credits and/or the preferred tax treatment of municipal obligations could also adversely affect the market value of municipal obligations. Since a large portion of our investment portfolio (51.7 percent at December 31, 2018) is invested in tax-exempt municipal obligations, any such changes in tax law could adversely affect the value of our investment portfolio.

We exercise prudence and significant judgment in analyzing and validating fair values, which are primarily provided by third parties, for securities in our investment portfolio, including those that are not regularly traded in active markets. We also exercise prudence and significant judgment in determining whether the impairment of particular investments is temporary or other-than-temporary. Due to the inherent uncertainties involved in these judgments, we may incur unrealized losses and subsequently conclude that other-than-temporary write downs of our investments are required.

***Our success depends primarily on our ability to underwrite risks effectively and adequately price the risks we underwrite.***

The results of our operations and our financial condition depend on our ability to underwrite and set premium rates accurately for a wide variety of determinable and indeterminable risks based on available information. Adequate rates are necessary to generate premiums sufficient to pay losses, loss settlement expenses and underwriting expenses and to earn a profit. To price our products accurately, we must collect and properly analyze a substantial amount of data; develop, test and apply appropriate pricing techniques; closely monitor and timely recognize changes in trends; and project both severity and frequency of losses with reasonable accuracy. We could underprice risks which would adversely affect our profit margins. Conversely, we could overprice risks which could reduce our sales volume and competitiveness. Our ability to undertake these efforts successfully, and to price our products accurately, is subject to a number of risks and uncertainties, including but not limited to:

- the availability of sufficient reliable data and our ability to properly analyze available data;
- market and competitive conditions;
- changes in medical care expenses and restoration costs;
- our selection and application of appropriate pricing techniques; and
- changes in the regulatory market, applicable legal liability standards and in the civil litigation system generally.

***The cyclical nature of the property and casualty insurance industry may affect our financial performance.***

The property and casualty insurance industry is cyclical in nature and has historically been characterized by soft markets (periods of relatively high levels of price competition, less restrictive underwriting standards and generally low premium rates) followed by hard markets (periods of capital shortages resulting in a lack of insurance availability, relatively low levels of price competition, more selective underwriting of risks and relatively high premium rates). During soft markets, we may lose business to competitors offering competitive insurance at lower prices. We may reduce our premiums or limit premium increases leading to a reduction in our profit margins and revenues. We expect these cycles to continue.

The demand for property and casualty insurance can also vary significantly, rising as the overall level of economic activity increases and falling as that activity decreases. Fluctuations in demand and competition could produce underwriting results that would have a negative impact on the results of our operations and financial condition.

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Ratings are an important factor in establishing the competitive position of insurance companies. Third-party rating agencies assess and rate the claims-paying ability, capital strength and creditworthiness of insurers and reinsurers based on criteria established by the agencies. A.M. Best rates our property and casualty insurance companies on a group basis. Since 2012, A.M. Best has also given an issuer credit rating to our parent holding company. The table below shows the current ratings assigned to our companies by A.M. Best.

	Financial Strength Rating	Issuer Credit Rating	Rating Held Since
Pooled Property and Casualty Companies	A	a	1994
United Fire Group, Inc.	N/A	bbb	2012

Financial strength and issuer credit ratings are used by policyholders, insurers, reinsurers and insurance and reinsurance intermediaries as an important means of assessing the financial strength, creditworthiness and quality of insurers and reinsurers. These ratings are not evaluations directed to potential purchasers of our common stock and are not recommendations to buy, sell or hold our common stock. These ratings are subject to change at any time and could be revised downward or revoked at the sole discretion of the rating agency. Downgrades in our financial strength ratings could adversely affect our ability to access the capital markets or could lead to increased borrowing costs in the future. Perceptions of the Company by investors, producers, other businesses and consumers could also be significantly impaired.

We believe that the ratings assigned by A.M. Best are an important factor in marketing our products. Our ability to retain our existing business and to attract new business in our insurance operations depends on our ratings by this agency. Our failure to maintain our ratings, or any other adverse development with respect to our ratings, could cause our current and future independent agents and policyholders to choose to transact their business with more highly rated competitors. If A.M. Best downgrades our ratings or publicly indicates that our ratings are under review, it is likely that we will not be able to compete as effectively with our competitors and our ability to sell insurance policies could decline, leading to a decrease in our premium revenue and earnings. For example, many of our agencies and policyholders have guidelines that require us to have an A.M. Best financial strength rating of "A-" or higher. A reduction of our A.M. Best ratings below "A-" would prevent us from issuing policies to a portion of our current policyholders or other potential policyholders with ratings requirements. Additionally, a ratings downgrade could materially increase the number of surrenders for all or a portion of the net cash values by the owners of policies and contracts we have issued, and materially increase the number of withdrawals by policyholders of cash values from their policies.

A reduction in our issuer credit rating could limit our ability to access capital markets or significantly increase the cost to us of raising capital. The failure of our insurance company subsidiaries to maintain their current ratings could dissuade a lender or reinsurance company from conducting business with us. A ratings downgrade could also cause some of our existing liabilities to be subject to acceleration, additional collateral support, changes in terms, or creation of additional financial obligations. It might also increase our interest or reinsurance costs.

***We are exposed to credit risk in certain areas of our operations.***

In addition to exposure to credit risk related to our investment portfolio, we are exposed to credit risk in several other areas of our business operations, including from:

- our reinsurers, who are obligated to us under our reinsurance agreements. See the risk factor titled "*Market conditions may affect our access to and the cost of reinsurance and our reinsurers may not pay losses in a timely manner, or at all,*" for a discussion of the credit risk associated with our reinsurance program;
- some of our independent agents, who collect premiums from policyholders on our behalf and are required to remit the collected premiums to us;
- some of our policyholders, which may be significant; and



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our surety insurance operations, where we guarantee to a third party that our bonded principal will satisfy certain performance obligations (for example, as in a construction contract) or certain financial obligations. If our policyholder defaults, we may suffer losses and be unable to be reimbursed by our policyholder.

To a large degree, the credit risk we face is a function of the economy; accordingly, we face a greater risk during periods of economic downturn. While we attempt to manage these risks through underwriting and investment guidelines, collateral requirements and other oversight mechanisms, our efforts may not be successful. For example, collateral obtained may subsequently have little or no value. As a result, our exposure to credit risk could materially and adversely affect our results of operation and financial condition.

***We are subject to comprehensive laws and regulations, changes to which may have an adverse effect on our financial condition and results of operations.***

Insurance is a highly regulated industry. We are subject to extensive supervision and regulation by the states in which we operate. As a public company, we are also subject to increased regulation at the federal level. Our ability to comply with these laws and regulations and obtain necessary and timely regulatory action is, and will continue to be, critical to our success and ability to earn profits.

Examples of regulations that pose particular risks to our ability to earn profits include the following:

***Required licensing.*** Our insurance company subsidiaries operate under licenses issued by various state insurance departments. If a regulatory authority were to revoke an existing license or deny or delay granting a new license, our ability to continue to sell insurance or to enter or offer new insurance products in that market would be substantially impaired.

***Regulation of insurance rates, fees and approval of policy forms.*** The insurance laws of most states in which we operate require insurance companies to file insurance premium rate schedules and policy forms for review and approval. When our loss ratio compares favorably to that of the industry, state regulatory authorities may resist or delay our efforts to raise premium rates, even if the property and casualty industry generally is not experiencing regulatory resistance to premium rate increases. If premium rate increases we deem necessary are not approved, we may not be able to respond to market developments and increased costs in that state. State regulatory authorities may even impose premium rate rollbacks or require us to pay premium refunds to policyholders, affecting our profitability. If insurance policy forms we seek to use are not approved by state insurance departments, our ability to offer new products and grow our business in that state could be substantially impaired.

***Restrictions on cancellation, nonrenewal or withdrawal.*** Many states have laws and regulations restricting an insurance company's ability to cease or significantly reduce its sales of certain types of insurance in that state, except pursuant to a plan that is approved by the state insurance departments. These laws and regulations could limit our ability to exit or reduce our business in unprofitable markets or discontinue unprofitable products. For example, the State of Louisiana has a law prohibiting the nonrenewal of homeowners policies written for longer than three years except under certain circumstances, such as for nonpayment of premium or fraud committed by the insured.

Additionally, our ability to adjust terms or increase pricing requires approval of regulatory authorities in certain states.

***Risk-based capital and capital adequacy requirements.*** Our insurance company subsidiaries and affiliate are subject to risk-based capital requirements that require us to report our results of risk-based capital calculations to state insurance departments and the NAIC. These standards apply specified risk factors to various asset, premium and reserve components of statutory capital and surplus reported in our statutory basis of accounting financial statements. Any failure to meet applicable risk-based capital requirements or minimum statutory capital requirements could subject us or our subsidiaries and affiliate to further examination or corrective action by state regulators, including limitations on our writing of additional business, state supervision or liquidation.

***Transactions between insurance companies and their affiliates.*** Transactions between us, our insurance company subsidiaries and our affiliates generally must be disclosed to, and in some cases approved by, state insurance departments. State insurance departments may refuse to approve or delay their approval of a transaction, which may impact our ability to innovate or operate efficiently.





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*Required participation in guaranty funds and assigned risk pools.* Certain states have enacted laws that require a property and casualty insurer conducting business in that state to participate in assigned risk plans, reinsurance facilities, and joint underwriting associations where participating insurers are required to provide coverage for assigned risks. The number of risks assigned to us by these plans is based on our share of total premiums written in the voluntary insurance market for that state. Pricing is controlled by the plan, often restricting our ability to charge the premium rate we might otherwise charge. Wherever possible, we utilize a designated servicing carrier to fulfill our obligations under these plans. Designated servicing carriers charge us fees to issue policies, adjust and settle claims and handle administrative reporting on our behalf. In these markets, we may be compelled to underwrite significant amounts of business at lower than desired premium rates, possibly leading to an unacceptable return on equity. While these facilities are generally designed so that the ultimate cost is borne by policyholders, the exposure to assessments and our ability to recoup these assessments through adequate premium rate increases may not offset each other in our financial statements. Moreover, even if they do offset each other, they may not offset each other in our financial statements for the same fiscal period, due to the ultimate timing of the assessments and recoupments or premium rate increases. Additionally, certain states require insurers to participate in guaranty funds to bear a portion of the unfunded obligations of impaired or insolvent insurance companies. These state funds periodically assess losses against all insurance companies doing business in the state. Our operating results and financial condition could be adversely affected by any of these factors.

*Restrictions on the amount, type, nature, quality and concentration of investments.* The various states in which we are domiciled have certain restrictions on the amount, type, nature, quality and concentration of our investments. Generally speaking, these regulations require us to be conservative in the nature and quality of our investments and restrict our ability to invest in riskier, but often higher yield investments. These restrictions may make it more difficult for us to obtain our desired investment results.

We benefit from certain tax items, including but not limited to, tax-exempt bond interest, dividends-received deductions, tax credits (such as foreign tax credits) and insurance reserve deductions. From time to time, the U.S. Congress, as well as foreign, state and local governments, considers legislation that could reduce or eliminate the benefits associated with these tax items. Recent federal tax reform may negatively impact our ability to take deductions that we made in the past.

*Terrorism Risk Insurance.* The Terrorism Risk Insurance Program Reauthorization Act of 2007 was signed into law on December 27, 2007. In January 2015, The Terrorism Risk Insurance Program Reauthorization Act of 2015 ("TRIPRA") was signed into law. TRIPRA extends the Terrorism Risk Insurance Program until December 31, 2020; gradually increases the coverage trigger for shared terrorism losses between the federal government and the insurance industry to \$200 billion per year (up from \$100 billion); and gradually increases the industry-wide retention to \$37.5 billion per year (up from \$27.5 billion). For further information about TRIPRA and its effect on our operations, refer to the information in the "Consolidated Results of Operations" section in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

*Accounting standards.* We prepare our consolidated financial statements in conformity with GAAP, which is periodically revised and/or expanded by recognized authoritative bodies, including the Financial Accounting Standards Board ("FASB"). These principles are subject to interpretation by the SEC and various other bodies formed to interpret and create appropriate accounting principles and guidance. Changes in GAAP and financial reporting requirements, or the interpretation of GAAP or those requirements, may have an impact on the content and presentation of our financial results and could have adverse consequences on our financial results, including lower reported results of operations and shareholders' equity and increased volatility and decreased comparability of our reported results with our historic results and with the results of other insurers. In addition, the required adoption of new accounting standards may result in significant incremental costs associated with initial implementation of and ongoing compliance with those standards. Additional information regarding recently proposed and adopted accounting standards and their potential impact on us is set forth in Note 1 "Summary of Significant Accounting Policies" to Part II, Item 8, "Financial Statements and Supplementary Data."



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*Corporate Governance and Public Disclosure Regulation.* Changing laws, regulations and standards relating to corporate governance and public disclosure, including Dodd-Frank, the Sarbanes-Oxley Act of 2002 and related SEC regulations, as well as the listing standards of the NASDAQ Stock Market, have created and are continuing to create uncertainty for public companies. While the federal government has not historically regulated the insurance business, in 2010 Dodd-Frank established a Federal Insurance Office within the U.S. Department of the Treasury. The Federal Insurance Office has limited regulatory authority and is empowered to gather data and information regarding the insurance industry and insurers, monitor aspects of the insurance industry, identify issues with regulation of insurers that could contribute to a systemic crisis in the insurance industry or the overall financial system, coordinate federal policy on international insurance matters and preempt state insurance measures under certain circumstances. While certain details and much of the impact of Dodd-Frank will not be known for some time, Dodd-Frank and other federal regulation adopted in the future may impose burdens on us, including impacting the ways we conduct our business, increasing compliance costs and duplicating state regulation. Additional regulation under these laws in the area of compensation disclosure, particularly regarding internal pay equity, officer and director hedging activities and compensation clawback policies is still expected.

Compliance with these laws and regulations requires us to incur administrative costs that decrease our profits. These laws and regulations may also prevent or limit our ability to underwrite and price risks accurately, obtain timely premium rate increases necessary to cover increased costs, discontinue unprofitable relationships or exit unprofitable markets and otherwise continue to operate our business profitably. In addition, our failure to comply with these laws and regulations could result in actions by state or federal regulators, including the imposition of fines and penalties or, in an extreme case, revocation of our ability to do business in one or more states. Finally, we could face individual, group and class action lawsuits by our policyholders and others for alleged violations of certain state laws and regulations. Each of these regulatory risks could have a negative effect on our profitability.

***Market conditions may affect our access to and the cost of reinsurance and our reinsurers may not pay losses in a timely manner, or at all.***

As part of our overall risk and capacity management strategy, we purchase reinsurance for significant amounts of the risk that we and our insurance company subsidiaries and affiliates underwrite, by transferring (or ceding) part of the risk we have assumed to a reinsurance company in exchange for part of the premium we receive in connection with the risk. These reinsurance arrangements diversify our business and reduce our exposure to large losses or from hazards of an unusual nature. As of December 31, 2018, we ceded premiums written of \$66.8 million to our reinsurers.

Although reinsurance makes the reinsurer liable to us to the extent the risk is transferred, it does not eliminate our liability to our policyholders because we remain liable as the direct insurer on all of the reinsured risks. As a result we are subject to credit risk relating to our ability to recover amounts due from our reinsurers.

Our ability to collect reinsurance recoverables may be subject to uncertainty. Our losses must meet the qualifying conditions of the reinsurance agreement. Our reinsurance agreements are subject to specified limits and we would not have reinsurance coverage to the extent that it exceeds those limits. We are also subject to the risk that reinsurers may dispute their obligations to pay our claims. Reinsurers must have the financial capacity and willingness to make payments under the terms of a reinsurance agreement or program. Reinsurers may dispute amounts we believe are due to us. Particularly, following a major catastrophic event, our inability to collect a material recovery from a reinsurer on a timely basis, or at all, could have a material adverse effect on our liquidity, operating results and financial condition. Market conditions determine the availability and cost of the reinsurance protection we purchase, which affects the level of our business profitability, as well as the level and types of risk we retain. Although we purposely work with several reinsurance intermediaries and reinsurers, we may be unable to maintain our current reinsurance facilities or obtain other reinsurance facilities in adequate amounts and at favorable premium rates. Moreover, there may be a situation in which we have more than two catastrophic events within one policy year. Because our current catastrophe reinsurance program only allows for one automatic reinstatement at an additional reinstatement premium, we would be required to obtain a new catastrophe reinsurance policy to maintain our current level of catastrophe reinsurance coverage. Such coverage may be difficult to obtain, particularly if it is necessary to do so during hurricane season following the second catastrophe. If we are unable to renew our expiring facilities or to



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obtain new reinsurance facilities, either our net exposure to risk will increase or, if we are unwilling to bear an increase in net risk exposures, we will have to reduce the amount of risk we underwrite.

***We face significant competitive pressures in our business that could cause demand for our products to fall or hinder our ability to introduce new products or services and keep pace with advances in technology, reducing our revenue and profitability.***

The insurance industry is highly competitive and will likely remain that way for the foreseeable future. In our property and casualty insurance business we compete, and will continue to compete, with many major U.S. and non-U.S. insurers and smaller regional companies, as well as mutual companies, specialty insurance companies, underwriting agencies, and diversified financial services companies, including banks, mutual funds, broker-dealers and asset-managers. Except for regulatory considerations, there are few barriers to entry in the insurance market. These developments may increase competition, by increasing the number, size and financial strength of competitors who may be able to offer, due to economies of scale, more competitive pricing than we can.

Our competitors may attempt to increase their market share by lowering rates. In that case, we could experience reductions in our underwriting margins or sales of insurance policies. Losing business to competitors offering similar products at lower prices or who have a competitive advantage may adversely affect the results of our operations. Additionally, economic conditions may reduce the total volume of business available to us and our competitors.

We price our insurance products based on estimated profit margins, and we may not be able to react in a timely manner to reprice our insurance products to respond to changes in the market. Some of our competitors may be larger and have far greater financial, technology and marketing resources than we do. If new or existing competitors decide to target our policyholder base by offering similar or enhanced product offerings or technologies at lower prices than we are able to offer, our premium revenue and our profitability could decline.

Our products are marketed exclusively through independent insurance agencies, most of which represent more than one company. We face competition within each agency and competition to retain qualified independent agents. Our competitors include companies that market their products through agents, as well as companies that sell insurance directly to their customers. In personal insurance, the use of comparative rating technologies has impacted our business and may continue to impact the entire industry. This has resulted in an increase in the total level of quote activity but a lower percentage of quotes have resulted in new business from customers. There is also the potential for similar technology to be used to compare rates for small business.

The successful implementation of our business model depends on our ability to adapt to evolving technologies and industry standards and introduce new products and services. There is no guarantee we will be able to introduce new or improved products, or that our products will achieve market acceptance. We may also not be successful in using new technologies effectively or adapting our proprietary technology to evolving customer requirements, causing our products or services to become obsolete.

Technology may be increasingly playing a role in our ability to be competitive. Innovations such as telematics and other usage-based methods of determining premiums may impact product design and pricing and may be an increasingly important factor in our ability to be competitive. Our competitive position may also be impacted by our ability to institute technology that collects and analyzes a wide variety of data points to make underwriting or other decisions.

***Our business depends on the uninterrupted operations of our facilities, systems and business functions.***

Our business depends on our employees' or vendors' ability to perform necessary business functions, such as processing new and renewal policies, providing customer service, making claims payments, facilitating collections and cancellations and performing actuarial functions necessary for pricing and product development. We increasingly rely on technology and systems to accomplish these business functions in an efficient and uninterrupted fashion. Our inability to access our facilities or a failure of technology, telecommunications or other systems could significantly impair our ability to perform such functions on a timely basis or affect the accuracy of transactions. If sustained or repeated, such a business interruption or system failure could result in a deterioration of our ability to write and process new and renewal business, serve our agents and policyholders or perform other necessary business functions as discussed above.



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If a natural disaster or a terrorist act occurs, our company and employees could be directly adversely affected, depending on the nature of the event. We have an emergency preparedness plan that consists of the information and procedures required to enable rapid recovery from an occurrence, such as natural disaster or business disruption, which could potentially disable us for an extended period of time. This plan was successfully tested during 2008 and 2016, both by the Midwest flooding that affected our corporate headquarters in Cedar Rapids, Iowa, and by Hurricane Ike in 2008 and Hurricane Harvey in 2017 that affected our Gulf Coast regional office in Galveston, Texas. It was also tested, to a lesser extent, by Super Storm Sandy in 2012 that affected our East Coast regional office in Pennington, New Jersey.

***Adverse capital and credit market conditions may significantly affect our ability to meet liquidity needs, as well as our access to and the cost of capital.***

Although capital market conditions have improved, our results of operations, financial condition, cash flows and statutory capital position could be materially adversely affected by continued volatility, uncertainty and disruptions in the capital and credit markets.

We maintain a level of cash and securities which, combined with expected cash inflows from investments and operations, is believed adequate to meet anticipated short-term and long-term benefit and expense payment obligations. In the event our current internal sources of liquidity do not satisfy our needs, we have entered into a \$50 million revolving unsecured credit facility that we can access, which also allows the Company to increase the aggregate amount of the commitments thereunder by up to \$100 million. The availability of additional financing will depend on a variety of factors such as market conditions, the general availability of credit, the volume of trading activities, the overall availability of credit to the financial services industry, our credit ratings and credit capacity as well as customers' or lenders' perception of our long- or short-term financial prospects. Similarly, our access to funds may be impaired if regulatory authorities or rating agencies take negative actions against us.

Disruptions, uncertainty or volatility in the capital and credit markets may limit our access to capital required to operate our business. Such market conditions may limit our ability to replace, in a timely manner, maturing liabilities; satisfy statutory capital requirements; and access the capital necessary to grow our business. As such, we may be forced to delay raising capital, issue shorter term securities than we prefer, utilize available internal resources or bear an unattractive cost of capital, which could decrease our profitability and significantly reduce our financial flexibility and liquidity.

***We may experience difficulty in integrating future acquisitions to our operations.***

The successful integration of any newly acquired businesses into our operations will require, among other things:

- the timely receipt of any required regulatory approvals;
- the retention and assimilation of their key management, sales and other personnel;
- the coordination of their lines of insurance products and services;
- the adaptation of their technology, information systems and other processes; and
- the retention and transition of their customers.

Unexpected difficulties in integrating any acquisition could result in increased expenses and the diversion of management time and resources. If we do not successfully integrate any acquired business into our operations, we may not realize the anticipated benefits of the acquisition, which could have a material adverse impact on our financial condition and results of operations. Further, any potential acquisitions may require significant capital outlays and, if we issue equity or convertible debt securities to pay for an acquisition, the issuance may be dilutive to our existing shareholders.

***The exclusions and limitations in our policies may not be enforceable.***

Many of the policies we issue include exclusions and other conditions that define and limit coverage, which exclusions and conditions are designed to manage our exposure to certain types of risks and expanding theories of legal liability. In addition, many of our policies limit the period during which a policyholder may bring a claim under the policy, which period in many cases is shorter than the statutory period under which these claims can be brought by our policyholders. While these exclusions and limitations help us assess and control our loss exposure, it





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is possible that a court or regulatory authority could nullify or void an exclusion or limitation, or legislation could be enacted which modifies or bars the use of these exclusions and limitations. This could result in higher than anticipated losses by extending coverage beyond the intent of our underwriting. In some instances, these changes may not become apparent until sometime after we have issued the insurance policies that are affected by these changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a policy is issued.

***Our internal controls are not fail-safe.***

As a result of the inherent limitations in all control systems, no system of controls can provide absolute assurance that all control objectives have been or will be met, and that every instance of error or fraud has been or will be detected. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system will be met. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of a simple error or mistake.

***The determination of the amount of impairments taken on our investments requires estimates and assumptions which are subject to differing interpretations and could materially impact our results of operations or financial position.***

The determination of the amount of impairments varies by investment type and is based upon our periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available. There can be no assurance that our management has accurately assessed the level of impairments taken in our financial statements. Furthermore, additional impairments may need to be taken in the future. Historical trends may not be indicative of future impairments.

Additionally, our management considers a wide range of factors about the instrument issuer and uses its best judgment in evaluating the cause of the decline in the estimated fair value of the instrument and in assessing the prospects for recovery. Inherent in management's evaluation of the security are assumptions and estimates about the operations of the issuer and its future earnings potential.

**Risks Relating to Our Common Stock**

***The ability of our subsidiaries to pay dividends may affect our liquidity and ability to meet our obligations.***

As a holding company, we have no significant independent operations of our own. Our principal sources of funds are dividends and other payments received from our subsidiaries. We rely on those dividends for our liquidity and to meet our obligations to pay dividends to shareholders and make share repurchases. Dividends from those subsidiaries depend on their statutory surplus, earnings and regulatory restrictions.

State insurance laws limit the ability of insurance subsidiaries to pay dividends and require our insurance subsidiaries to maintain specified minimum levels of statutory capital and surplus. The actual ability to pay dividends may further be constrained by business and regulatory considerations, such as the impact of dividends on surplus, by our competitive position and by the amount of premiums that we can write. Ordinary dividend payments, or dividends that do not require prior approval by the insurance subsidiaries' domiciliary state insurance regulator are generally limited to amounts determined by a formula which varies by jurisdiction. Extraordinary dividends, on the other hand, require prior regulatory approval by the insurance subsidiaries' domiciliary state insurance regulator before they can be made. In addition, competitive pressures generally require insurance companies to maintain insurance financial strength ratings. These restrictions and other regulatory requirements affect the ability of our insurance subsidiaries to make dividend payments to us. At times we may not be able to pay dividends on our common stock, or we may be required to seek prior approval from the applicable regulatory authority before we can pay any such dividends. In addition, the payment of dividends by us is within the discretion of our Board of Directors and will depend on numerous factors, including our financial condition, our capital requirements and other factors that our Board of Directors considers relevant.

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***The price of our common stock may be volatile.***

The trading price of our common stock may fluctuate substantially due to a variety of factors, some of which are beyond our control and may not be related to our operating performance. These fluctuations could be significant and could cause a loss in the amount invested in our shares of common stock. Factors that could cause fluctuations include, but are not limited to, the following:

- variations in our actual or anticipated operating results or changes in the expectations of financial market analysts with respect to our results;
- investor perceptions of the insurance industry in general and the Company in particular;
- market conditions in the insurance industry and any significant volatility in the market;
- major catastrophic events; and
- departure of key personnel.

***Certain provisions of our organizational documents, as well as applicable insurance laws, could impede an attempt to replace or remove our management or members of our Board of Directors, prevent the sale of the Company or prevent or frustrate any attempt by shareholders to change the direction of the Company, each of which could diminish the value of our common stock.***

Our articles of incorporation and bylaws, as well as applicable laws governing corporations and insurance companies, contain provisions that could impede an attempt to replace or remove our management or prevent the sale of the Company that, in either case, shareholders might consider being in their best interests. For example:

- our Board of Directors is divided into three classes. At any annual meeting of our shareholders, our shareholders have the right to appoint approximately one-third of the directors on our Board of Directors. Consequently, it will take at least two annual shareholder meetings to effect a change in control of our Board of Directors;
- our articles of incorporation limit the rights of shareholders to call special shareholder meetings;
- our articles of incorporation set the minimum number of directors constituting the entire Board of Directors at nine and the maximum at 15, and they require approval of holders of 60.0 percent of all outstanding shares to amend these provisions. Within the range, the Board of Directors may increase by one each year the number of directors serving on the Board of Directors;
- our articles of incorporation require the affirmative vote of 60.0 percent of all outstanding shares to approve any plan of merger, consolidation, or sale or exchange of all, or substantially all, of our assets;
- our Board of Directors may fill vacancies on the Board of Directors;
- our Board of Directors has the authority, without further approval of our shareholders, to issue shares of preferred stock having such rights, preferences and privileges as the Board of Directors may determine;
- Section 490.1110 of the Iowa Business Corporation Act imposes restrictions on mergers and other business combinations between us and any holder of 10.0 percent or more of our common stock; and
- Section 490.624A of the Iowa Business Corporation Act authorizes the terms and conditions of stock rights or options issued by us to include restrictions or conditions that preclude or limit the exercise, transfer, or receipt of such rights or options by a person, or group of persons, owning or offering to acquire a specified number or percentage of the outstanding common shares or other securities of the corporation.

Further, the insurance laws of Iowa and the states in which our insurance company subsidiaries are domiciled prohibit any person from acquiring direct or indirect control of us or our insurance company subsidiaries, generally defined as owning or having the power to vote 10.0 percent or more of our outstanding voting stock, without the prior written approval of state regulators.

These provisions of our articles of incorporation and bylaws, and these state laws governing corporations and insurance companies, may discourage potential acquisition proposals. These provisions and state laws may also delay, deter or prevent a change of control of the Company, in particular through unsolicited transactions that some

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or all of our shareholders might consider to be desirable. As a result, efforts by our shareholders to change the direction or the Company's management may be unsuccessful, and the existence of such provisions may adversely affect market prices for our common stock if they are viewed as discouraging takeover attempts.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Our headquarters are located in Cedar Rapids, Iowa, where we own approximately 183,000 square feet of office and building space that is ready to occupy. We are in the process of constructing improvements to our Cedar Rapids facilities. In addition, we own and lease office and building space, including underwriting and claims offices, throughout the U.S. We believe our existing facilities, both owned and leased, are in good condition and suitable for the conduct of our business.

**ITEM 3. LEGAL PROCEEDINGS**

In the normal course of its business, the Company is a party to a variety of legal proceedings. While the final outcome of these legal proceedings cannot be predicted with certainty, management believes all of the proceedings pending as of December 31, 2018 to be ordinary and routine and does not expect these legal proceedings to have a material adverse effect on the Company's financial position or results of operations.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

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**PART II.**

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

**Common Shareholders**

United Fire Group, Inc.'s common stock is traded on the NASDAQ stock market under the symbol "UFCS." On February 26, 2019, there were 701 holders of record of United Fire Group, Inc. common stock. The number of record holders does not reflect shareholders who beneficially own common stock in nominee or street name, but does include participants in our employee stock purchase plan.

**Dividends**

Our practice has been to pay quarterly cash dividends, which we have paid every quarter since March 1968.

As a holding company with no independent operations of its own, United Fire Group, Inc. relies on dividends received from its insurance company subsidiaries in order to pay dividends to its common shareholders. Dividends payable by our insurance subsidiaries are governed by the laws in the states in which they are domiciled. In all cases, these state laws permit the payment of dividends only from earned surplus arising from business operations. For example, under Iowa law, the maximum dividend or distribution that may be paid within a 12-month period without prior approval of the Iowa Insurance Commissioner is generally restricted to the greater of 10 percent of statutory surplus as of the preceding December 31, or net income of the preceding calendar year on a statutory basis, not greater than earned statutory surplus. Other states in which our insurance company subsidiaries are domiciled may impose similar restrictions on dividends and distributions. Based on these restrictions, at December 31, 2018, our insurance company subsidiary, United Fire & Casualty, is able to make a maximum of \$106.2 million in dividend payments without prior regulatory approval. On June 20, 2018, the Company sought approval from the Iowa Insurance Commissioner for a proposed ordinary dividend of \$50.7 million and extraordinary dividend of \$39.3 million, for a total of \$90.0 million. The Company received approval from Iowa Insurance Commissioner on July 9, 2018 and subsequently paid a \$3.00 per share special dividend or a total of \$75.2 million to shareholders on August 20, 2018.

Payments of any future dividends and the amounts of such dividends will depend upon factors such as net income, financial condition, capital requirements, and general business conditions. We will only pay dividends if declared by our Board of Directors out of legally available funds and there can be no assurance that we will continue to pay such dividends or the amount of such dividends.

Additional information about these restrictions is incorporated by reference from Note 6 "Statutory Reporting, Capital Requirements and Dividends and Retained Earnings Restrictions" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**Issuer Purchases of Equity Securities**

Under our share repurchase program, we may purchase our common stock from time to time on the open market or through privately negotiated transactions. The amount and timing of any purchases will be at our discretion and will depend upon a number of factors, including the share price, general economic and market conditions, and corporate and regulatory requirements. Our share repurchase program may be modified or discontinued at any time.

The following table provides information with respect to purchases of shares of common stock made by or on our behalf or by any "affiliated purchaser," as defined in Rule 10b-18(a)(3) under the Exchange Act, during the year ended December 31, 2018:

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Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as a Part of Publicly Announced Plans or Programs	Maximum Number of Shares that may yet be Purchased Under the Plans or Programs
1/1/18 - 1/31/18	—	\$ —	—	2,236,572
2/1/18 - 2/28/18	115,372	44.89	115,372	2,121,200
3/1/18 - 3/31/18	5,000	44.98	5,000	2,116,200
4/1/18 - 4/30/18	—	—	—	2,116,200
5/1/18 - 5/31/18	—	—	—	2,116,200
6/1/18 - 6/30/18	—	—	—	2,116,200
7/1/18 - 7/31/18	—	—	—	2,116,200
8/1/18 - 8/31/18	—	—	—	2,116,200
9/1/18 - 9/30/18	—	—	—	2,116,200
10/1/18 - 10/31/18	—	—	—	2,116,200
11/1/18 - 11/30/18	—	—	—	2,116,200
12/1/18 - 12/31/18	—	—	—	2,116,200
Total	120,372		120,372	

(1) Our share repurchase program was originally announced in August 2007. In August 2016, our Board of Directors authorized the repurchase of up to an additional 1,500,000 shares of common stock through the end of August 2018. This is in addition to the 1,528,886 shares of common stock remaining under its previous authorizations. In August 2018, our Board of Directors extended our share repurchase program through the end of August, 2020. As of December 31, 2018 we remained authorized to repurchase 2,116,200 shares of common stock through the end of August 2020.

**United Fire Group, Inc. Common Stock Performance Graph**

The following graph compares the performance of an investment in United Fire Group Inc.'s common stock from December 31, 2013 through December 31, 2018, with the Standard & Poor's 500 Index ("S&P 500 Index"), and the Standard & Poor's 600 Property and Casualty Index ("S&P 600 P&C Index"). The graph assumes \$100 was invested on December 31, 2013 in our common stock and each of the below listed indices and that all dividends were reinvested on the date of payment without payment of any commissions. Dollar amounts in the graph are rounded to the nearest whole dollar. The performance shown in the graph represents past performance and should not be considered an indication of future performance.

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The following table shows the data used in the total return performance graph above.

	Period Ended					
Index	12/31/13	12/31/14	12/31/15	12/31/16	12/31/17	<b>12/31/18</b>
United Fire Group, Inc.	\$ 100.00	\$ 106.59	\$ 140.99	\$ 185.10	\$ 175.92	<b>\$ 230.54</b>
S&P 500 Index	100.00	113.69	115.26	129.05	157.22	<b>150.33</b>
S&P 600 P&C Index	100.00	105.14	120.82	151.23	165.01	<b>176.62</b>

The foregoing performance graph is being furnished as part of this Annual Report on Form 10-K solely in accordance with the requirement under Rule 14a-3(b)(9) to furnish our shareholders with such information, and therefore, shall not be deemed to be filed or incorporated by reference into any filings by the Company under the Securities Act or Exchange Act.

**ITEM 6. SELECTED FINANCIAL DATA**

The following table sets forth certain selected financial data derived from the Consolidated Financial Statements of United Fire Group, Inc. and its subsidiaries and affiliates. The data should be read in conjunction with Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Part II, Item 8, "Financial Statements and Supplementary Data."

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(In Thousands, Except Per Share Data)

As of and for the years Ended December 31	2018	2017	2016	2015	2014
<b>Balance Sheet Data:</b>					
Total cash and investments - continuing operations	\$2,138,577	\$1,984,495	\$1,860,978	\$1,737,161	\$1,621,356
Total assets					
Continuing operations	2,816,698	2,597,297	2,449,140	2,280,674	2,127,623
Assets held for sale	—	1,586,134	1,605,618	1,609,702	1,729,066
Total assets	2,816,698	4,183,431	4,054,758	3,890,376	3,856,689
Losses and loss settlement expenses	1,312,483	1,224,183	1,123,896	1,003,895	969,437
Unearned premiums - continuing operations	492,918	465,391	443,802	414,971	378,635
Total liabilities					
Continuing operations	1,928,323	1,862,923	1,722,651	1,606,869	1,540,416
Liabilities held for sale	—	1,347,135	1,390,223	1,404,610	1,498,858
Total liabilities	1,928,323	3,210,058	3,112,874	3,011,479	3,039,274
Net unrealized investment gains (loss), after tax	(9,323 )	214,865	133,892	128,369	149,623
Repurchase of United Fire Group, Inc. common stock	(5,404 )	(29,784 )	(3,746 )	(2,423 )	(12,942 )
Total stockholders' equity	888,375	973,373	941,884	878,897	817,415
Book value per share	35.40	39.06	37.04	34.94	32.67
<b>Income Statement Data from Continuing Operations:</b>					
Revenues					
Net premiums earned	\$1,037,451	\$997,492	\$936,131	\$851,695	\$766,939
Investment income, net of investment expenses	52,894	51,190	55,284	46,559	44,236
Net realized investment gains (losses)	(20,179 )	4,055	4,947	1,124	4,177
Other income (loss)	—	—	—	(107 )	911
Revenues	1,070,166	1,052,737	996,362	899,271	816,263
Losses and loss settlement expenses	731,611	725,713	652,433	520,087	509,811
Amortization of deferred policy acquisition costs	206,232	207,746	202,892	180,183	161,310
Other underwriting expenses	141,473	103,628	83,540	83,631	79,117
Net income	2,255	44,870	49,918	85,320	52,376
Combined ratio <sup>(1)</sup>	104.0	% 104.0	% 100.3	% 92.0	% 97.8
<b>Income Statement Data from Discontinued Operations:</b>					
Net premiums earned	\$13,003	\$61,368	\$87,270	\$79,195	\$61,391
Investment income	12,663	49,720	51,538	54,222	60,373
Revenues	24,755	115,713	140,585	135,647	125,631
Losses and loss settlement expenses	10,823	40,451	31,365	29,001	26,432
Increase in liability for future policy benefits	5,023	27,632	59,969	50,945	36,623
Other underwriting expenses	3,864	13,281	19,881	19,306	15,754
Interest on policyholders' accounts	4,499	18,525	20,079	23,680	30,245
Net income (loss)	(1,912 )	6,153	786	3,806	6,761
<b>Earnings Per Share Data:</b>					
Continuing operations:					
Basic earnings per common share	\$0.09	\$1.79	\$1.94	\$3.41	\$2.07
Diluted earnings per common share	0.09	1.75	1.90	3.38	2.05
Discontinued operations:					
Basic earnings per common share	(0.08 )	0.24	0.03	0.15	0.27
Diluted earnings per common share	(0.07 )	0.24	0.03	0.15	0.27
<b>Other Supplemental Data:</b>					

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Cash dividends declared per common share	<b>\$4.21</b>	\$1.09	\$0.97	\$0.86	\$0.78
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(1) The combined ratio is a commonly used financial measure of property and casualty underwriting performance. A combined ratio below 100.0 percent generally indicates a profitable book of business.



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**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following Management's Discussion and Analysis should be read in conjunction with Part II, Item 6, "Selected Financial Data" and Part II, Item 8, "Financial Statements and Supplementary Data." Amounts (except per share amounts) are presented in thousands, unless otherwise noted.

**FORWARD-LOOKING STATEMENTS**

It is important to note that our actual results could differ materially from those projected in any forward-looking statements in this Form 10-K. Please refer to "Forward-Looking Information" and Part I, Item 1A, "Risk Factors" of this report for information concerning factors that could cause actual results to differ materially from the forward-looking statements contained in this Form 10-K.

**BUSINESS OVERVIEW**

Originally founded in 1946 as United Fire & Casualty Company, United Fire Group, Inc. and its consolidated insurance company subsidiaries provide insurance protection for individuals and businesses through several regional companies. Our property and casualty insurance company subsidiaries are licensed in 46 states plus the District of Columbia and are represented by approximately 1,100 independent agencies.

**Discontinued Operations**

On September 18, 2017, the Company signed a definitive agreement to sell its subsidiary, United Life, to Kuvare and on March 30, 2018, the sale closed. As a result, our life insurance business, previously a separate segment, was considered held for sale and reported as discontinued operations in the Consolidated Financial Statements. All periods presented have been revised to show results from continuing and discontinued operations, unless otherwise noted. For more information, refer to Part II, Item 8, Note 17 "Discontinued Operations."

**Reportable Segments**

Prior to the announcement of the sale of our life insurance business, we have historically reported our operations in two business segments, each with a wide range of products:

• property and casualty insurance, which includes commercial lines insurance, personal lines insurance and assumed reinsurance; and

• life insurance, which includes deferred and immediate annuities, universal life products and traditional life (primarily single premium whole life) insurance products.

We managed these businesses separately, as they generally do not share the same customer base, and each has different products, pricing, and expense structures.

Subsequent to the announcement of the sale of our life insurance business on September 19, 2017, we operate and report one business segment, which contains our continuing operations. Our life insurance business was considered held for sale and reported as discontinued operations throughout this Form 10-K, unless otherwise noted. For more information, refer to Part II, Item 8, Note 10 "Segment Information."

**Pooling Arrangement**

All of our property and casualty insurance subsidiaries are members of an intercompany reinsurance pooling arrangement. The Company's pooling arrangement permits the participating companies to rely on the capacity of the entire pool's capital and surplus, rather than being limited to policy exposures of a size commensurate with each

participant's own surplus level.

Table of Contents**Geographic Concentration****Continuing Operations - Property and Casualty Insurance Business**

For 2018, approximately 48.9 percent of our property and casualty statutory direct premiums written were written in Texas, California, Iowa, Missouri and Colorado.

In 2018, 2017 and 2016 the direct statutory premiums written by our property and casualty insurance operations were distributed as follows:

(In Thousands)	Years Ended December 31,			% of Total		
	2018	2017	2016	2018	2017	2016
Texas	<b>\$193,953</b>	\$178,314	\$156,926	<b>17.4</b>	% 16.7	% 15.6
California	<b>124,473</b>	123,285	117,669	<b>11.2</b>	11.6	11.7
Iowa	<b>98,128</b>	100,826	105,948	<b>8.8</b>	9.5	10.5
Missouri	<b>70,646</b>	64,746	58,964	<b>6.4</b>	6.1	5.9
Colorado	<b>56,152</b>	53,981	47,678	<b>5.1</b>	5.1	4.7
New Jersey	<b>52,037</b>	49,305	52,232	<b>4.7</b>	4.6	5.2
Minnesota	<b>49,491</b>	50,432	51,033	<b>4.4</b>	4.7	5.1
Louisiana	<b>44,007</b>	39,849	38,219	<b>4.0</b>	3.7	3.8
Illinois	<b>40,431</b>	41,042	43,666	<b>3.6</b>	3.9	4.3
All Other States	<b>382,385</b>	363,427	333,788	<b>34.4</b>	34.1	33.2
Direct Statutory Premiums Written	<b>\$1,111,703</b>	\$1,065,207	\$1,006,123	<b>100.0</b>	% 100.0	% 100.0

**Discontinued Operations - Life Insurance Business**

Our life insurance subsidiary marketed its products primarily in the Midwest, East Coast and West. In 2018, 2017 and 2016 the direct statutory premiums written by our life insurance operations were distributed as follows:

(In Thousands)	Years Ended December 31,			% of Total		
	2018	2017	2016	2018	2017	2016
Iowa	<b>\$9,951</b>	\$40,773	\$41,559	<b>31.3</b>	% 32.5	% 30.1
Wisconsin	<b>3,578</b>	14,897	12,578	<b>11.3</b>	11.9	9.1
Illinois	<b>3,227</b>	10,872	12,481	<b>10.2</b>	8.7	9.0
Nebraska	<b>2,572</b>	10,197	10,351	<b>8.1</b>	8.1	7.5
Minnesota	<b>2,003</b>	12,201	14,289	<b>6.3</b>	9.7	10.3
All Other States	<b>10,432</b>	36,581	47,014	<b>32.8</b>	29.1	34.0
Direct Statutory Premiums Written	<b>\$31,763</b>	\$125,521	\$138,272	<b>100.0</b>	% 100.0	% 100.0

**Sources of Revenue and Expense**

We evaluate profit or loss based upon operating and investment results. Profit or loss described in the following sections of this Management's Discussion and Analysis is reported on a pre-tax basis. Our primary sources of revenue are premiums and investment income. Major categories of expenses include losses and loss settlement expenses, future policy benefits, underwriting and other operating expenses and interest on policyholders' accounts.

**Profit Factors**

Our profitability is influenced by many factors, including price, competition, economic conditions, investment returns, interest rates, catastrophic events and other natural disasters, man-made disasters, state regulations, court decisions, and changes in the law. To manage these risks and uncertainties, we seek to achieve consistent profitability through strong agency relationships, exceptional customer service, fair and prompt claims handling,

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disciplined underwriting, superior loss control services, prudent management of our investments, appropriate matching of assets and liabilities, effective use of ceded reinsurance and effective and efficient use of technology.

**MEASUREMENT OF RESULTS**

Our consolidated financial statements are prepared on the basis of GAAP. We also prepare financial statements for each of our insurance company subsidiaries based on statutory accounting principles and file them with insurance regulatory authorities in the states where they do business.

Management evaluates our operations by monitoring key measures of growth and profitability. We believe that disclosure of certain non-GAAP financial measures enhances investor understanding of our financial performance.

The following provides further explanation of the key measures management uses to evaluate our results:

**Catastrophe losses** is a commonly used non-GAAP financial measure which utilizes the designations of the Insurance Services Office ("ISO") and are reported with losses and loss settlement expense amounts net of reinsurance recoverables, unless specified otherwise. According to the ISO, a catastrophe loss is defined as a single unpredictable incident or series of closely related incidents that result in \$25.0 million or more in U.S. industry-wide direct insured losses to property and that affect a significant number of insureds and insurers ("ISO catastrophe"). In addition to ISO catastrophes, we also include as catastrophes those events ("non-ISO catastrophes"), which may include U.S. or international losses, that we believe are, or will be, material to our operations, either in amount or in number of claims made. Management, at times, may determine for comparison purposes of our financial results that it is more meaningful to exclude extraordinary catastrophe losses and resulting litigation. The frequency and severity of catastrophic losses we experience in any year affect our results of operations and financial position. In analyzing the underwriting performance of our property and casualty insurance business, we evaluate performance both including and excluding catastrophe losses. Portions of our catastrophe losses may be recoverable under our catastrophe reinsurance agreements. We include a discussion of the impact of catastrophes because we believe it is meaningful for investors to understand the variability in our periodic earnings.

	Years Ended December		
	31,		
(In Thousands)	2018	2017	2016
ISO catastrophes	\$46,757	\$66,421	\$57,932
Non-ISO catastrophes <sup>(1)</sup> (64 )		7,618	3,299
Total catastrophes	\$46,693	\$74,039	\$61,231

(1) Includes international assumed losses.

Table of Contents**RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2018, 2017 AND 2016****FINANCIAL HIGHLIGHTS**

<i>(In Thousands)</i>	Years Ended December 31,			% Change	
	2018	2017	2016	2018 vs. 2017	2017 vs. 2016
<b>Revenues</b>					
Net premiums earned	\$1,037,451	\$997,492	\$936,131	4.0 %	6.6 %
Investment income, net of investment expenses	52,894	51,190	55,284	3.3	(7.4 )
Net realized investment gains (losses)					
Change in the value of equity securities	(21,994 )	332	301	NM	10.3
All other net realized gains	1,815	3,723	4,646	(51.2 )	(19.9)
Net realized investment gains (losses)	(20,179 )	4,055	4,947	NM	(18.0)
<b>Total revenues</b>	<b>\$1,070,166</b>	<b>\$1,052,737</b>	<b>\$996,362</b>	<b>1.7 %</b>	<b>5.7 %</b>
<b>Benefits, losses and expenses</b>					
Losses and loss settlement expenses	\$731,611	\$725,713	\$652,433	0.8 %	11.2 %
Amortization of deferred policy acquisition costs	206,232	207,746	202,892	(0.7 )	2.4
Other underwriting expenses	141,473	103,628	83,540	36.5	24.0
<b>Total benefits, losses and expenses</b>	<b>\$1,079,316</b>	<b>\$1,037,087</b>	<b>\$938,865</b>	<b>4.1 %</b>	<b>10.5 %</b>
<b>Income (loss) from continuing operations before income taxes</b>	<b>\$ (9,150 )</b>	<b>\$ 15,650</b>	<b>\$ 57,497</b>	<b>(158.5)%</b>	<b>(72.8)%</b>
Federal income tax expense (benefit)	(11,405 )	(29,220 )	8,379	(61.0 )%	NM
<b>Net income from continuing operations</b>	<b>\$2,255</b>	<b>\$44,870</b>	<b>\$49,118</b>	<b>(95.0)%</b>	<b>(8.6)%</b>
<b>Income (loss) from discontinued operations, net of tax</b>	<b>(1,912 )</b>	<b>6,153</b>	<b>786</b>	<b>(131.1)%</b>	<b>NM</b>
<b>Gain on sale of discontinued operations, net of tax</b>	<b>27,307</b>	<b>—</b>	<b>—</b>	<b>NM</b>	<b>— %</b>
<b>Net income</b>	<b>\$27,650</b>	<b>\$51,023</b>	<b>\$49,904</b>	<b>(45.8)%</b>	<b>2.2 %</b>
<b>GAAP Ratios:</b>					
Net loss ratio (without catastrophes)	66.0	% 65.4	% 63.2	% 0.9	% 3.5 %
Catastrophes - effect on net loss ratio	4.5	% 7.4	% 6.5	% (39.2 )%	13.8 %
Net loss ratio <sup>(1)</sup>	70.5	% 72.8	% 69.7	% (3.2 )%	4.4 %
Expense ratio <sup>(2)</sup>	33.5	% 31.2	% 30.6	% 7.4	% 2.0 %
Combined ratio <sup>(3)</sup>	104.0	% 104.0	% 100.3	% —	% 3.7 %

NM = not meaningful

(1) The net loss ratio is calculated by dividing the sum of losses and loss settlement expenses by net premiums earned. We use the net loss ratio as a measure of the overall underwriting profitability of the insurance business we write and to assess the adequacy of our pricing. Our net loss ratio is meaningful in evaluating our financial results as reported in our Consolidated Financial Statements.

(2) The expense ratio is calculated by dividing nondeferred underwriting expenses and amortization of deferred policy acquisition costs by net premiums earned. The expense ratio measures a company's operational efficiency in producing, underwriting and administering its insurance business.

(3) The combined ratio is a commonly used financial measure of property and casualty underwriting performance. A combined ratio below 100.0 percent generally indicates a profitable book of business. The combined ratio is the sum of the net loss ratio and the underwriting expense ratio.

In 2018, the decrease in net income from continuing operations compared to 2017 is due to the decrease in the fair value of equity securities and an increase in other underwriting expenses partially offset by an increase in net premiums earned. The decrease in the fair value of equity securities was the result of volatile equity markets in the fourth quarter 2018. The increase in other underwriting expenses is primarily due to our continued investment in our

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multi-year Oasis project to upgrade our technology platform to enhance core underwriting decisions, selection of risks and productivity. The increase in net premiums earned is due to organic growth from a combination of new business and geographical expansion and from rate increases.

In 2017, our net income benefited from the Tax Cuts and Jobs Act ("Tax Act"), which resulted in a tax benefit of \$21.9 million for the year. Income from continuing operations before income taxes decreased 72.8 percent, from 2016, primarily driven by an 11.2 percent increase in losses and loss settlement expenses due to an increase in catastrophe losses and deterioration of our core loss ratio. A portion of this deterioration was driven by an increase in large losses, which we define as losses greater than \$500 thousand, in our commercial automobile lines of business in the first three quarters of 2017. Also contributing to the decrease in income from continuing operations before income taxes was an increase in other underwriting expenses due to a deterioration in the profitability of the commercial and personal auto lines of business, which limits the amount of expenses which can be deferred into our deferred acquisition costs, partially offset by a decrease in post-retirement benefit expenses. These increases were partially offset by a 6.6 percent increase in net premiums earned.

**Premiums from continuing operations**

The following table shows our premiums written and earned from continuing operations for 2018, 2017 and 2016:

(In Thousands)				% Change	
	2018	2017	2016	2018 vs. 2017	2017 vs. 2016
Years ended December 31,					
Direct premiums written	<b>\$1,111,703</b>	\$ 1,065,207	\$ 1,006,123	<b>4.4</b> %	5.9 %
Assumed premiums written	<b>16,761</b>	15,179	16,834	<b>10.4</b>	(9.8 )
Ceded premiums written	<b>(66,800 )</b>	(61,273 )	(57,988 )	<b>9.0</b>	5.7
Net premiums written <sup>(1)</sup>	<b>\$1,061,664</b>	\$ 1,019,113	\$ 964,969	<b>4.2</b> %	5.6 %
Less: change in unearned premiums	<b>(27,527 )</b>	(21,588 )	(28,829 )	<b>(27.5)</b>	25.1
Less: change in prepaid reinsurance premiums	<b>3,314</b>	(33 )	(9 )	<b>NM</b>	(266.7)
Net premiums earned	<b>\$1,037,451</b>	\$ 997,492	\$ 936,131	<b>4.0</b> %	6.6 %

NM = not meaningful

(1) **Net premiums written:** Net premiums written is a non-GAAP measure. While not a substitute for any GAAP measure of performance, net premiums written is frequently used by industry analysts and other recognized reporting sources to facilitate comparisons of the performance of insurance companies. Net premiums written are the amount charged for insurance policy contracts issued and recognized on an annualized basis at the effective date of the policy. Management believes net premiums written are a meaningful measure for evaluating insurance company sales performance and geographical expansion efforts. Net premiums written for an insurance company consists of direct premiums written and reinsurance assumed, less reinsurance ceded. Net premiums earned is calculated on a pro rata basis over the terms of the respective policies. Unearned premium reserves are established for the portion of premiums written applicable to the unexpired term of insurance policy in force. The difference between net premiums earned and net premiums written is the change in unearned premiums and change in prepaid reinsurance premiums.

**Net Premiums Written**

Net premiums written comprise direct and assumed premiums written, less ceded premiums written. Direct premiums written are the total policy premiums, net of cancellations, associated with policies issued and underwritten by our property and casualty insurance business. Assumed premiums written are the total premiums associated with the insurance risk transferred to us by other insurance and reinsurance companies pursuant to reinsurance contracts. Ceded premiums written is the portion of direct premiums written that we cede to our reinsurers under our reinsurance contracts. Net premiums earned are recognized ratably over the life of a policy and differ from net premiums written, which are recognized on the effective date of the policy.

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*Direct Premiums Written*

Direct premiums written from continuing operations increased \$46.5 million in 2018 as compared to 2017 due to organic growth from a combination of new business and geographical expansion and from rate increases. Written and earned premium growth were within management's expectations of 3 percent to 5 percent growth.

Direct premiums written from continuing operations increased \$59.1 million in 2017 as compared to 2016 due to organic growth from a combination of new business and geographical expansion. Written and earned premium growth were within management's expectations of 4 percent to 6 percent growth.

*Assumed Premiums Written*

Assumed premiums written increased \$1.6 million in 2018 as compared to 2017 due to an increase in cedant premium growth. In 2018, we renewed our participation in all of our assumed programs.

Assumed premiums written decreased \$1.7 million in 2017 as compared to 2016 due to a drop in reinsurance rates. In 2017, we renewed our participation in all of our assumed programs.

*Ceded Premiums Written*

Direct and assumed premiums written are reduced by the ceded premiums that we pay to reinsurers. For 2018, we ceded 9.0 percent more premiums to reinsurers as a result of continued growth in direct premiums written. For 2017, we ceded 5.7 percent more premiums to reinsurers as a result of continued growth in direct premiums written offset by declining ceded reinsurance rates.

***Losses and Loss Settlement Expenses from continuing operations***

*Catastrophe Exposures*

Catastrophe losses are inherent risks of the property and casualty insurance business. Catastrophic events include, without limitation, hurricanes, tornadoes, earthquakes, hailstorms, wildfires, high winds, winter storms and other natural disasters, along with man-made exposures to losses resulting from, without limitation, acts of war, acts of terrorism and political instability. Such events result in insured losses that can be, and may continue to be, a material factor in our results of operations and financial position, as the extent of losses from a catastrophe is a function of both the total amount of insured exposure in an area affected by the event and the severity of the event. Because the level of insured losses that may occur in any one year cannot be accurately predicted, these losses contribute to fluctuations in our year-to-year results of operations and financial position. Some types of catastrophes are more likely to occur at certain times within the year than others, which adds an element of seasonality to our property and casualty insurance claims. Our property and casualty insurance business experiences some seasonality with regard to premiums written, which are generally highest in January and July and lowest during the fourth quarter. Losses and loss settlement expenses incurred tend to remain consistent throughout the year, with the exception of catastrophe losses, which generally are highest in the second and third quarters. The frequency and severity of catastrophic events are difficult to accurately predict in any year. However, some geographic locations are more susceptible to these events than others. We control our direct insurance exposures in regions that are prone to naturally occurring catastrophic events through a combination of geographic diversification, restrictions on the amount and location of new business production in such regions, and reinsurance. We regularly assess our concentration of risk exposures in natural catastrophe exposed areas. We have strategies and underwriting standards to manage these exposures through individual risk selection, subject to regulatory constraints, and through the purchase of catastrophe reinsurance coverage. We use catastrophe modeling and a risk concentration management tool to monitor and control our accumulations of potential losses in natural catastrophe exposed areas of the United States, such as the Gulf and East Coasts, as well as in areas of exposure in other countries where we are exposed to a portion of an insurer's underwriting risk under our assumed reinsurance contracts.

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Overall, the models indicate increased risk estimates for our exposure to hurricanes in the U.S., but the impact of the models on our book of business varies significantly among the regions that we model for hurricanes. Based on our analysis, we have implemented more targeted underwriting and rate initiatives in some regions. We will continue to take underwriting actions and/or purchase additional reinsurance as necessary to reduce our exposure.

Catastrophe modeling generally relies on multiple inputs based on experience, science, engineering and history, and the selection of those inputs requires a significant amount of judgment. The modeling results may also fail to account for risks that are outside the range of normal probability or are otherwise unforeseen. Because of this, actual results may differ materially from those derived from our modeling assumptions.

Despite our efforts to manage our catastrophe exposure, the occurrence of one or more severe natural catastrophic events in heavily populated areas could have a material effect on our results of operations, financial condition or liquidity.

The process of estimating and establishing reserves for losses incurred from catastrophic events is inherently uncertain and the actual ultimate cost of a claim, net of reinsurance recoveries, may vary materially from the estimated amount reserved. Although we reinsure a portion of our exposure, reinsurance may prove to be inadequate if a major catastrophic event exceeds our reinsurance limits or if we experience a number of small catastrophic events that individually fall below our reinsurance retention level.

*Catastrophe Losses*

In 2018, our pre-tax catastrophe losses were \$46.7 million, a decrease as compared to \$74.0 million and \$61.2 million in 2017 and 2016, respectively. In 2018, our catastrophe losses included 46 catastrophes with our largest pre-tax catastrophe losses coming from the California wildfires, which totaled \$9.2 million. Catastrophe losses in 2018 added 4.5 percentage points to the combined ratio, which is below our historical 10-year average of 6.4 percentage points.

In 2017, the increase in catastrophe losses was primarily due to hurricanes (Harvey, Irma, Maria) in the third quarter and destructive California wildfires in the second half of the year. In 2017, our catastrophe losses included 50 catastrophes and our largest single pre-tax catastrophe loss totaled \$9.0 million. Catastrophe losses in 2017 added 7.4 percentage points to the combined ratio. In 2016, our catastrophe losses included 41 catastrophes, where our largest single pre-tax catastrophe loss totaled \$10.4 million. Catastrophe losses in 2016 added 6.5 percentage points to the combined ratio.

*Catastrophe Reinsurance*

In 2018, 2017 and 2016, we did not exceed our catastrophe reinsurance retention level of \$20.0 million per event. We use many reinsurers, both domestic and foreign, which helps us to avoid concentrations of credit risk associated with our reinsurance. All reinsurers we do business with must meet the following minimum criteria: capital and surplus of at least \$250.0 million and an A.M. Best rating or an S&P rating of at least "A-." If a reinsurer is rated by both rating agencies, then both ratings must be at least an "A-."



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The following table represents the primary reinsurers we utilize and their financial strength ratings as of December 31, 2018:

Name of Reinsurer	A.M. Best S&P Rating	
Aspen Insurance UK Limited	A+	A
General Reinsurance Corporation <sup>(2)</sup>	A++	AA+
Hannover Rueckversicherung AG <sup>(1) (2)</sup>	A+	AA-
Lloyd's	A	A+
Munich Re <sup>(2)</sup>	A+	AA-
Odyssey Re <sup>(2)</sup>	A	A-
Partner Re <sup>(1)(2)</sup>	A+	A+
QBE Reinsurance Corporation <sup>(1)</sup>	A	A+
R&V Versicherung AG <sup>(2)</sup>	N/A	AA-
Renaissance Re	A	A+
SCOR Reinsurance Company <sup>(1)(2)</sup>	A	A+
Toa Re <sup>(1)</sup>	A+	A+
Tokio Marine Kiln	A	A+
Transatlantic Re <sup>(1)</sup>	A	A+

(1) Primary reinsurers participating in the property and casualty excess of loss programs.

(2) Primary reinsurers participating in the surety excess of loss program.

Refer to Part II, Item 8, Note 4 "Reinsurance" for further discussion of our reinsurance programs.

*Terrorism Coverage*

The Terrorism Risk Insurance Program Reauthorization Act of 2007 was signed into law on December 27, 2007. In January 2015, TRIPRA was signed into law. TRIPRA extends the Terrorism Risk Insurance Program until December 31, 2020; gradually increases the coverage trigger for shared terrorism losses between the federal government and the insurance industry to \$200 billion per year (up from \$100 billion); and gradually increases the industry-wide retention to \$37.5 billion per year (up from \$27.5 billion). TRIPRA coverage includes most direct commercial lines of business, including coverage for losses from nuclear, biological and chemical exposures if coverage was afforded by an insurer, with exclusions for commercial automobile insurance, burglary and theft insurance, surety, professional liability insurance and farm owners multiple peril insurance. Under TRIPRA, each insurer has a deductible amount, which is 20.0 percent of the prior year's direct commercial lines earned premiums for the applicable lines of business, and retention of 15.0 percent above the deductible. No insurer that has met its deductible shall be liable for the payment of any portion of that amount that exceeds the annual aggregate loss cap specified in TRIPRA. TRIPRA provides marketplace stability. As a result, coverage for terrorist events in both the insurance and reinsurance markets is often available. The amount of aggregate losses necessary for an act of terrorism to be certified by the U.S. Secretary of Treasury, the Secretary of State and the Attorney General was \$100.0 million for 2018 and remains the same for 2019. Our TRIPRA deductible was \$136.4 million for 2018 and our TRIPRA deductible is expected to be \$137.3 million for 2019. Our catastrophe and non-catastrophe reinsurance programs provide limited coverage for terrorism exposure excluding nuclear, biological and chemical-related claims.

*2018 Results*

In 2018, our losses and loss settlement expenses were 0.8 percent higher than 2017 and our net loss ratio decreased 2.3 points. The decrease in our net loss ratio was due to a decrease in catastrophe losses slightly offset by a deterioration in our core loss ratio. Catastrophe losses decreased to \$46.7 million in both our direct business and assumed reinsurance business as compared to \$74.0 million in 2017. The deterioration in our core loss ratio was 0.6 percent, which was primarily driven by an increase in severity of losses in our other liability line of business from auto related bodily injury claims.

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### *2017 Results*

In 2017, our losses and loss settlement expenses were 11.2 percent higher than 2016 and our net loss ratio increased 3.1 points due to an increase in catastrophe losses, which accounted for 0.9 percentage points of the increase, and an increase in large losses over \$500 thousand in our commercial automobile lines of business in the first three quarters of 2017 and an increase in losses in our personal lines of business, primarily in personal auto and fire and allied lines of business. Catastrophe losses increased to \$74.0 million in both our direct business and assumed reinsurance business as compared to \$61.2 million in 2016.

### *2016 Results*

In 2016, our losses and loss settlement expenses were 25.4 percent higher than 2015 and our net loss ratio increased 8.7 points due to an increase in catastrophe losses, which accounted for 2.7 percentage points of the increase, and an increase in large losses over \$500 thousand in our commercial automobile and commercial fire & allied lines of business.

### *Reserve Development*

For many liability claims, significant periods of time, ranging up to several years, and for certain construction defect claims, more than a decade, may elapse between the occurrence of the loss, the reporting of the loss to us and the settlement or other disposition of the claim. As a result, loss experience in the more recent accident years for the long-tail liability coverages has limited statistical credibility in our reserving process because a relatively small proportion of losses in these accident years are reported claims and an even smaller proportion are paid losses. In addition, long-tail liability claims are more susceptible to litigation and can be significantly affected by changing contract interpretations and the legal environment. Consequently, the estimation of loss reserves for long-tail coverages is more complex and subject to a higher degree of variability. Reserves for these long-tail coverages represent a significant portion of our overall carried reserves.

When establishing reserves and monitoring reserve adequacy, we analyze historical data and consider the potential impact of various loss development factors and trends including historical loss experience, legislative enactments, judicial decisions, legal developments in imposition of damages, experience with alternative dispute resolution, results of our medical bill review process and changes and trends in general economic conditions, including the effects of inflation. All of these factors influence our estimates of required reserves and for long-tail lines these factors can change over the course of the settlement of the claim. However, there is no precise method for evaluating the specific dollar impact of any individual factor on the development of reserves.

Our reserving philosophy is to reserve claims to their ultimate expected loss amount as soon as practicable after information about a claim becomes available. This approach tends to produce, on average, prudently conservative case reserves, which we expect to result in some level of favorable development over the course of settlement.

### *2018 Development*

The property and casualty insurance business experienced \$54.2 million of favorable development in our net reserves for prior accident years for the year ended December 31, 2018. The majority of favorable development came from four lines, workers' compensation with \$27.0 million favorable development, reinsurance assumed with \$15.6 million favorable development, commercial automobile with \$9.5 million favorable development, and fidelity and surety with \$2.8 million favorable development. The only individual line with unfavorable development was commercial liability with \$3.7 million of unfavorable development. Workers' compensation favorable development was primarily from reserve reductions for both reported claims and loss IBNR which were more than sufficient to offset paid loss with additional favorable development coming from loss adjustment expenses ("LAE") where the LAE IBNR reduction was more than sufficient to offset paid LAE which continues to benefit from additional litigation management efforts when compared to prior years. Reinsurance assumed favorable development is attributable reductions in reserves for both reported claims and loss IBNR as we reviewed our book of business and



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released excess reserves during 2018. Commercial automobile favorable development was driven by loss adjustment expense where LAE IBNR reductions were more than sufficient to offset paid LAE. Fidelity and surety favorable development is attributable to reductions in reserves for both reported claims and loss IBNR which were more than sufficient to offset paid loss. Commercial liability adverse development is attributable to reserve strengthening for both reported claims and loss IBNR primarily in response to an increase in umbrella auto related claims while loss adjustment expense developed favorably with reductions of LAE IBNR more than sufficient to offset paid LAE.

*2017 Development*

The property and casualty insurance business experienced \$54.3 million of favorable development in our net reserves for prior accident years for the year ended December 31, 2017. The majority of favorable development came from two lines, commercial liability with \$35.1 million favorable development and workers' compensation with \$19.2 million favorable development, partially offset by \$6.3 million of unfavorable development for assumed reinsurance. All other lines combined \$6.3 million favorable development with no single line experiencing more than \$3.7 million of development, either favorable or unfavorable. Much of the favorable long-tail liability development continues to come from loss adjustment expense and is attributed to our continued litigation management efforts. There was also a reduction in reserves for incurred but not reported claims because our long tail liability has experienced fewer late reported claims than what was initially anticipated. The favorable workers' compensation development is due to the combination of reductions in reserves for reported claims and reductions in reserves for incurred but not reported claims for both loss and loss adjustment expense.

*2016 Development*

The property and casualty insurance business experienced \$31.2 million of favorable development in our net reserves for prior accident years for the year ended December 31, 2016. The majority of favorable development came from two lines: commercial liability with \$25.4 million of favorable development and workers' compensation with \$12.2 million of favorable development. The favorable development was offset by unfavorable development from commercial fire & allied lines with \$6.4 million of unfavorable development and commercial automobile with \$5.5 million of unfavorable development. During the twelve-month period ended December 31, 2016 all other lines combined development was \$5.5 million of favorable development. The favorable development for the year ended December 31, 2016, is attributable to reductions in reserves for loss adjustment expense which continues to benefit from successful management of litigation expenses.

Reserve development amounts can vary significantly from year-to-year depending on a number of factors, including the number of claims settled and the settlement terms, and are subject to reallocation between accident years and lines of business.

Table of Contents**Net Loss Ratios by Line**

The following table depicts our net loss ratios for 2018, 2017 and 2016:

<i>(In Thousands)</i>	Years ended December 31, 2018			2017			2016		
	Net Premiums Earned	Net Losses and Loss Settlement Expenses Incurred	Net Loss Ratio	Net Premiums Earned	Net Losses and Loss Settlement Expenses Incurred	Net Loss Ratio	Net Premiums Earned	Net Losses and Loss Settlement Expenses Incurred	Net Loss Ratio
Commercial lines									
Other liability	\$311,931	\$183,692	58.9 %	\$306,480	\$121,054	39.5 %	\$289,982	\$130,748	45.1 %
Fire and allied lines	234,612	165,097	70.4	227,711	178,768	78.5	221,758	176,961	79.8
Automobile	284,274	271,248	95.4	250,465	266,272	106.3	214,009	211,882	99.0
Workers' compensation	95,203	57,601	60.5	104,166	71,053	68.2	103,605	74,051	71.5
Fidelity and surety	24,437	1,878	7.7	24,981	2,206	8.8	22,507	222	1.0
Other	1,728	449	26.0	1,829	312	17.1	1,745	498	28.5
Total commercial lines	\$952,185	\$679,965	71.4 %	\$915,632	\$639,665	69.9 %	\$853,606	\$594,362	69.6 %
Personal lines									
Fire and allied lines	\$41,581	\$32,959	79.3 %	\$43,005	\$34,503	80.2 %	\$43,463	\$27,402	63.0 %
Automobile	29,247	25,016	85.5	27,046	28,997	107.2	25,207	23,123	91.7
Other	1,210	(213)	(17.6)	1,159	268	23.1	1,090	260	23.9
Total personal lines	\$72,038	\$57,762	80.2 %	\$71,210	\$63,768	89.5 %	\$69,760	\$50,785	72.8 %
Reinsurance assumed	\$13,228	\$(6,116)	(46.2) %	\$10,650	\$22,280	209.2 %	\$12,765	\$7,286	57.1 %
Total	\$1,037,451	\$731,611	70.5 %	\$997,492	\$725,713	72.8 %	\$936,131	\$652,433	69.7 %

NM=Not meaningful

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***Commercial Lines***

The net loss ratio in our commercial lines of business, excluding assumed reinsurance, was 71.4 percent in 2018 compared to 69.9 percent in 2017 and 69.6 percent in 2016. The net loss ratio in 2018 is up slightly compared to 2017 with a deterioration in our other liability line of business from an increase in auto related bodily injury claims due to an adverse litigious environment. The net loss ratio in 2017 as was comparable to 2016 with an increase in losses in commercial auto and fidelity and surety offset by decreases in other liability and workers' compensation.

***Other Liability***

Other liability is business insurance covering bodily injury and property damage arising from general business operations, accidents on the insured's premises and products manufactured or sold. Because of the long-tail nature of liability claims, significant periods of time, ranging up to several years, may elapse between the occurrence of the loss, the reporting of the loss to us and the settlement of the claim.

In recent years, we began to use our loss control department more extensively in an attempt to return this line of business to a higher level of profitability. For example, our loss control department has representatives who make multiple visits each year to businesses and job sites to ensure safety. We also do not renew accounts that no longer meet our underwriting or pricing guidelines. We avoid accounts that have become too underpriced for the risk.

***Construction Defect Losses***

Incurred losses from construction defect claims were \$15.9 million in 2018 compared to \$15.7 million and \$10.4 million in 2017 and 2016, respectively. At December 31, 2018, we had \$44.5 million in construction defect loss and loss settlement expense reserves (excluding IBNR reserves which are calculated at the overall other liability commercial line), which consisted of 2,706 claims. In comparison, at December 31, 2017, we had reserves of \$34.4 million, excluding IBNR reserves, consisting of 1,857 claims. The increase in the incurred losses is due to continued improvement in the economic environment which increases construction activity. Our West Coast and Rocky Mountain regions continue to be the origin of the majority of the construction defect claim activity.

Construction defect claims generally relate to allegedly defective work performed in the construction of structures such as apartments, condominiums, single family dwellings or other housing, as well as the sale of defective building materials. Such claims seek recovery due to damage caused by alleged deficient construction techniques or workmanship. The reporting of such claims can be quite delayed due to an extended statute of limitations, sometimes up to ten years. Court decisions have expanded insurers' exposure to construction defect claims as well. Defense costs are also a part of the insured expenses covered by liability policies and can be significant, sometimes greater than the cost of the actual paid claims.

We have exposure to construction defect liabilities in Colorado and surrounding states. We have historically insured small- to medium-sized contractors in this geographic area. In an effort to limit the number of future claims from multi-unit buildings, we implemented policy exclusions in 2009, later revised in 2010, that exclude liability coverage for contractors performing "residential structural" operations on any building project with more than 12 units or on single family homes in any subdivision where the contractor is working on more than 15 homes. The exclusions do not apply to remodeling or repair of an existing structure. We also changed our underwriting guidelines to add a professional liability exclusion when contractors prepare their own design work or blueprints and implemented the multi-family exclusion and tract home building limitation form for the state of Colorado and our other western states as a means to reduce our exposure in future years. When offering commercial umbrella coverage for structural residential contractors, limits of liability are typically limited to a maximum of \$2.0 million per occurrence. Requests to provide additional insured status for "developers" are declined.

As a result of our acquisition of Mercer Insurance Group in 2011, we added construction defect exposure in the states of California, Nevada and Arizona. Mercer Insurance Group has been writing in these states for more than 20 years. In order to minimize our exposure to construction defect claims in this region, we continually review the coverage we offer and our pricing models. In an effort to limit our exposure from residential multi-unit buildings, we started including condominium and townhouse construction policy exclusions in 2012 for our contracting policies in



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this region. For the majority of our residential contractors we limit the size of any tracts the contractor is working on to 25 homes or less and do not include a continuous trigger with our designated work exclusion. In a majority of the policies in our small service, repair and remodel contractors program, we have a favorable new residential construction exclusion. We also apply strict guidelines when additional insured forms are required and changed our underwriting guidelines to limit our exposure to large, multi-party construction defect claims.

***Commercial Fire and Allied Lines***

Commercial fire and allied lines include fire, allied lines, commercial multiple peril and inland marine. The insurance covers losses to an insured's property, including its contents, from weather, fire, theft or other causes. We provide this coverage through a variety of business policies.

The net loss ratio improved 8.1 percentage points in 2018 compared to 2017. The improvement in 2018 is attributable to a decrease in catastrophe losses, a decrease in frequency of claims partially offset by an increase in severity of losses, a decrease in paid losses and a lower increase in reserves for incurred but not reported claims. The net loss ratio in 2017 was comparable to 2016, with a slight improvement 1.3 percentage points.

***Commercial Automobile***

Our commercial automobile insurance covers physical damage to an insured's vehicle, as well as liabilities to third parties. Automobile physical damage insurance covers loss or damage to vehicles from collision, vandalism, fire, theft, flood or other causes. Automobile liability insurance covers bodily injury, damage to property resulting from automobile accidents caused by the insured, uninsured or underinsured motorists and the legal costs of defending the insured against lawsuits.

The net loss ratio improved 10.9 percentage points in 2018 compared to 2017. This improvement is attributable to a decrease in frequency of losses along with favorable changes in loss reserves for reported claims and loss IBNR compared to the same period in 2017. We continue to make steady progress in improving our core loss ratio, however, the performance of this line of business remains below our expectations. Our strategy to improve profitability continues to be: aggressively seeking rate increases, focusing on loss control initiatives and taking action on underperforming accounts. The deterioration in our commercial automobile insurance line in 2017 as compared to 2016 was due to an increase in the number of severe losses of claims in the first three quarters of 2017.

***Workers' Compensation***

We consider our workers' compensation business to be a companion product; we rarely write stand-alone workers' compensation policies. Our workers' compensation insurance covers primarily small- to mid-size accounts. The net loss ratio improved 7.7 percentage points in 2018 compared to 2017. The improvement in 2018 is attributable to a lower increase in reserves for reported claims during 2018 as compared to 2017. The improvement in our workers' compensation line of business in 2017 as compared to 2016 was due to the presence of relatively stronger claim reserves for prior accident years. As claims were paid and closed the release of reserves for reported claims was more than sufficient to offset claim payments.

Although we have seen steady improvement in the net loss ratio for the last two years in our worker's compensation line of business, competitive market conditions continued in 2018, putting downward pressure on rates. The challenges faced by workers' compensation insurance providers to attain profitability include the regulatory climates in some states that make it difficult to obtain appropriate premium rate increases and inflationary medical costs. Consequently, we have increased the utilization of our loss control unit in the analysis of current risks, with the intention of increasing the quality of our workers' compensation book of business. We are currently using these modeling analytics to assist us in risk selection, and we will continue to evaluate the model results.

***Fidelity and Surety***

Our surety products guarantee performance and payment by our bonded principals. Our contract bonds protect owners from failure to perform on the part of our principals. In addition, our surety bonds protect material suppliers and subcontractors from nonpayment by our contractors. When surety losses occur, our loss is determined by



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estimating the cost to complete the remaining work and to pay the contractor's unpaid bills, offset by contract funds due to the contractor, reinsurance, and the value of any collateral to which we may have access.

The net loss ratio improved 1.1 percentage points in 2018 compared to 2017. This improvement is attributable to a decrease in reserves for reported claims in 2018 compared to an increase in 2017. In 2017, the change in the loss ratio was primarily due to claims from a large contractor's bankruptcy which occurred during the fourth quarter. During 2017 the claims from the large contractor's bankruptcy exceed our \$1.5 million reinsurance retention level.

***Personal Lines***

Our personal lines consist primarily of fire and allied lines (including homeowners) and automobile lines. The net loss ratio improved 9.3 percentage points in 2018 compared to 2017. This improvement was primarily driven by our personal auto line of business due to a decrease in frequency and severity of paid losses and reserves for reported claims. In 2017 our net loss ratio deteriorated 16.7 percentage points as compared to 2016. The 2017 deterioration is attributable to increased frequency and severity for personal automobile as well as an increase in the volume of claims from homeowners.

For our personal lines, we use the CATography™ Underwriter tool, which gives us the ability to determine whether the premium we charge for an exposure is adequate in areas where hurricanes and earthquakes occur. We have also implemented predictive analytics and data prefill for our personal automobile line. Data prefill is a data accessing methodology that allows for a more complete profile of our customers at the agent's point of sale during the quotation process.

***Assumed Reinsurance***

Our assumed reinsurance is the business we choose to write by participating in programs insuring insurance companies. The net loss ratio decreased in 2018 compared to 2017 as we remain conservative in our reserving approach, and during the year we reviewed our book of business and released excess reserves. The net loss ratio deteriorated in 2017, as compared to 2016, primarily due to expected claims from three hurricanes (Harvey, Irma, and Maria) as well as expected claims from California wildfires.

In 2018, 2017 and 2016, we renewed our participation in all of our assumed programs.

***Other Underwriting Expenses***

Our underwriting expense ratio, which is a percentage of other underwriting expenses over net premiums earned, was 33.5 percent, 31.2 percent and 30.6 percent for 2018, 2017, and 2016, respectively. The underwriting expense ratio increased in 2018 primarily due to our continued investment in our multi-year Oasis project to upgrade our technology platform to enhance core underwriting decisions, selection of risks and productivity.

The underwriting expense ratio increased in 2017 primarily due to a deterioration in the profitability of the commercial and personal auto lines of business, which limits the amount of expenses which can be deferred into our deferred acquisition costs, partially offset by a decrease in post-retirement benefit expenses.



Table of Contents**Discontinued Operations Results**

	<b>Years Ended December 31,</b>			<b>% Change</b>	
	<b>2018</b>	2017	2016	<b>2018 vs. 2017</b>	2017 vs. 2016
<i>(In Thousands)</i>					
<b>Revenues</b>					
Net premiums earned	<b>\$13,003</b>	\$61,368	\$87,270	<b>(78.8 )%</b>	(29.7 )%
Investment income, net	<b>12,663</b>	49,720	51,538	<b>(74.5 )%</b>	(3.5 )%
Net realized investment gains (losses)	<b>(1,057 )</b>	4,008	1,156	<b>(126.4 )%</b>	246.7 %
Other income	<b>146</b>	617	621	<b>(76.3 )%</b>	(0.6 )%
Total revenues	<b>\$24,755</b>	\$115,713	\$140,585	<b>(78.6 )%</b>	(17.7 )%
<b>Benefits, Losses and Expenses</b>					
Losses and loss settlement expenses	<b>\$10,823</b>	\$40,451	\$31,365	<b>(73.2 )%</b>	29.0 %
Increase in liability for future policy benefits	<b>5,023</b>	27,632	59,969	<b>(81.8 )%</b>	(53.9 )%
Amortization of deferred policy acquisition costs	<b>1,895</b>	5,181	8,121	<b>(63.4 )%</b>	(36.2 )%
Other underwriting expenses	<b>3,864</b>	13,281	19,881	<b>(70.9 )%</b>	(33.2 )%
Interest on policyholders' accounts	<b>4,499</b>	18,525	20,079	<b>(75.7 )%</b>	(7.7 )%
Total benefits, losses and expenses	<b>\$26,104</b>	\$105,070	\$139,415	<b>(75.2 )%</b>	(24.6 )%
<b>Income (loss) before income taxes</b>	<b>\$ (1,349 )</b>	\$10,643	\$1,170	<b>(112.7 )%</b>	NM

NM =Not meaningful

The sale of our discontinued operations closed on March 30, 2018, and therefore income was only earned in the first quarter of 2018. For the year ended December 31, 2018, our discontinued operations had a loss before income taxes of \$1.3 million, compared to income before income taxes of \$10.6 million and \$1.2 million for the same period of 2017 and 2016, respectively.

**Federal Income Taxes**

We reported a federal income tax benefit on a consolidated basis of \$3.3 million or 13.5 percent of pre-tax income in 2018. In 2017, we reported a federal income tax benefit on a consolidated basis of \$24.7 million or 94.1 percent of pre-tax income and federal income tax expense of \$8.8 million or 14.9 percent of pre-tax income in 2016. In 2017 our effective tax rate was impacted by the Tax Act, which was enacted on December 22, 2017. The Tax Act significantly revised the U.S. corporate income tax laws including lowering the U.S. federal corporate tax rate from 35% to 21% effective January 1, 2018. Our effective federal tax rate varied from the statutory federal income tax expense rate in each year, due primarily to our portfolio of tax-exempt securities.

In December 2017, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 118, which addresses how a company recognizes provisional amounts when a company does not have the necessary information available, prepared or analyzed in reasonable detail to complete its accounting for the effect of the changes in the Tax Act. The measurement period ends when a company has obtained, prepared and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. As of December 31, 2018 we have completed accounting for the tax effects of enactment of the Tax Act, and no adjustment was made during the measurement period.

Due to our determination that we may not be able to fully realize the benefits of the net operating loss ("NOL") acquired in the purchase of American Indemnity Financial Corporation, which are only available to offset the future taxable income of our property and casualty insurance operations and are further limited as to the amount that can be utilized in any given year, we have recorded a valuation allowance against these NOLs. Based on a yearly review, we determine whether the benefit of the NOLs can be realized, and, if so, the decrease in the valuation allowance is recorded as a reduction to current federal income tax expense. If NOLs expire during the year, the decrease in the valuation allowance is offset with a corresponding decrease to the deferred income tax asset. The valuation allowance was reduced by \$0.7 million in 2018 due to the realization of \$3.1 million in NOLs. During 2018, the remaining NOL

from the purchase of American Indemnity Financial Corporation was fully realized.

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As of December 31, 2018, we had no alternative minimum tax credit carryforwards.

### **INVESTMENTS**

#### **Investment Environment**

The investment landscape experienced a meaningful transition in 2018. Overall, U.S. economic fundamentals were strong, as robust labor markets, easing regulatory costs and solid growth provided a good tailwind to both business and consumer sentiment. In spite of an early jump in volatility due to factors more technical than fundamental in nature, risk assets traded higher through most of the year, however, the mood among investors shifted dramatically in the fourth quarter because of tightening financial condition and although the broad economic backdrop remained positive, signs the economy may be cooling emerged. The uncertainty prompted a significant increase in market volatility, and most every major global asset class produced negative total returns in 2018 in spite of healthy performance for three quarters of the year. The S&P 500 Index lost 14 percent in the fourth quarter to close the year down 6.2 percent. Treasury yields were higher year-over-year, though well-inside peak levels reached in November when the US 10 year Treasury Rate hit 3.25 percent. Cash was the rare market segment that traded to the positive for the year.

Overall, the current environment is challenging given the cross currents investors are faced with. On the constructive side, robust wage gains are supportive of consumer activity which constitutes over two-thirds of total economic output. In addition, small business optimism and hiring data is showing this portion of the economy to be upbeat and robust. Although corporate defaults remain benign and earnings stable, tremors are being felt more widespread in lower quality sectors. As such, investment yields are higher than a year ago with Treasury rates and credit risk premiums elevated. By and large, the balance of risks is neutral to slightly negative as we head into a new year. Our investment program is defensive in nature, and designed to outperform during periods of market uncertainty.

#### **Investment Philosophy**

The Company's assets are invested to preserve capital and maximize after-tax returns while maintaining an appropriate balance of risk. The return on our portfolio is an important component of overall financial results, but quality and safety of principal is the highest priority of our investment program. Our general investment philosophy is to purchase financial instruments with the expectation that we will hold them to their maturity. However, active management of our portfolio is considered necessary to appropriately manage risk, achieve portfolio objectives and maximize investment income as market conditions change.

We work with our insurance company subsidiaries to develop an appropriate investment strategy that aligns with their business needs and supports United Fire's strategic plan and risk appetite. The portfolio is structured so as to be in compliance with state insurance laws that prescribe the quality, concentration and type of investments that may be made by insurance companies. All but a very small portion of our investment portfolio is managed internally.

#### **Investment Portfolio**

Our invested assets from continuing operations at December 31, 2018 totaled \$2.1 billion, compared to \$1.9 billion at December 31, 2017, an increase of \$185.2 million. At December 31, 2018, fixed maturity securities and equity securities comprised 85.0 percent and 12.0 percent of our investment portfolio, respectively. Because the primary purpose of the investment portfolio is to fund future claims payments, we utilize a conservative investment philosophy, investing in a diversified portfolio of high-quality, intermediate-term taxable corporate bonds, taxable U.S. government and government agency bonds and tax-exempt U.S. municipal bonds. Our overall investment strategy is to stay fully invested (i.e., minimize cash balances). If additional cash is needed we have an ability to borrow funds available under our revolving credit facility.



Table of Contents**Composition**

We develop our investment strategies based on a number of factors, including estimated duration of reserve liabilities, short- and long-term liquidity needs, projected tax status, general economic conditions, expected rates of inflation and regulatory requirements. We administer our investment portfolio based on investment guidelines approved by management and the investment committee of our Board of Directors that comply with applicable statutory regulations.

The composition of our investment portfolio at December 31, 2018 is presented at carrying value in the following table:

<i>(In Thousands)</i>	Total	Percent of Total
Fixed maturities:		
Available-for-sale	\$1,749,488	84.4 %
Trading securities	13,240	0.6
Equity securities	248,361	12.0
Mortgage loans	25,782	1.2
Other long-term investments	37,077	1.8
Short-term investments	175	—
Total	\$2,074,123	100.0%

At December 31, 2018, we classified \$1.7 billion, or 99.2 percent, of our fixed maturities portfolio as available-for-sale, compared to \$1.5 billion, or 98.9 percent, at December 31, 2017. Available-for-sale fixed maturity securities are carried at fair value, with changes in fair value recognized as a component of accumulated other comprehensive income in stockholders' equity. We record fixed maturity trading securities, primarily convertible redeemable preferred debt securities, and equity securities at fair value, with any changes in fair value recognized in earnings.

As of December 31, 2018 and 2017, we did not have direct exposure to investments in subprime mortgages or other credit enhancement vehicles.

**Credit Quality**

The following table shows the composition of fixed maturity securities held in our available-for-sale, held-to-maturity and trading security portfolios by credit rating for both continuing and discontinued operations at December 31, 2018 and 2017. Information contained in the table is generally based upon the issue credit ratings provided by Moody's, unless the rating is unavailable, in which case we obtain it from Standard & Poor's.

<i>(In Thousands)</i>	<b>December 31, 2018</b>		<b>December 31, 2017</b>	
Rating	<b>Carrying Value</b>	<b>% of Total</b>	<b>Carrying Value</b>	<b>% of Total</b>
AAA	<b>\$734,471</b>	<b>41.7 %</b>	\$885,000	29.7 %
AA	<b>684,863</b>	<b>38.9</b>	839,210	28.1
A	<b>178,282</b>	<b>10.1</b>	616,787	20.7
Baa/BBB	<b>157,349</b>	<b>8.9</b>	585,968	19.6
Other/Not Rated	<b>7,763</b>	<b>0.4</b>	55,156	1.9
	<b>\$1,762,728</b>	<b>100.0 %</b>	\$2,982,121	100.0%

**Duration**

Our investment portfolio is invested primarily in fixed maturity securities whose fair value is susceptible to market risk, specifically interest rate changes. Duration is a measurement used to quantify our inherent interest rate risk and



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analyze our ability to match our invested assets to our reserve liabilities. If our invested assets and reserve liabilities have similar durations, then any change in interest rates will have an equal effect on these accounts. The primary purpose for matching invested assets and reserve liabilities is liquidity. With appropriate matching, our investments will mature when cash is needed, preventing the need to liquidate other assets prematurely. Mismatches in the duration of assets and liabilities can cause significant fluctuations in our results of operations.

The weighted average effective duration of our portfolio of fixed maturity securities was 5.1 years at December 31, 2018 compared to 5.0 years at December 31, 2017.

The amortized cost and fair value of available-for-sale and trading fixed maturity securities at December 31, 2018, by contractual maturity, are shown in the following table. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Asset-backed securities, mortgage-backed securities and collateralized mortgage obligations may be subject to prepayment risk and are therefore not categorized by contractual maturity.

<i>(In Thousands)</i>	Available-For-Sale		Trading	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
December 31, 2018				
Due in one year or less	\$48,331	\$48,492	\$4,408	\$5,232
Due after one year through five years	225,816	226,069	5,019	5,872
Due after five years through 10 years	544,551	542,662	—	—
Due after 10 years	691,968	684,274	1,850	2,136
Asset-backed securities	3,256	3,495	—	—
Mortgage-backed securities	7,642	7,424	—	—
Collateralized mortgage obligations	239,725	237,072	—	—
	\$1,761,289	\$1,749,488	\$11,277	\$13,240

**Investment Results**

We invest the premiums received from our policyholders in order to generate investment income, which is an important component of our revenues and profitability. The amount of investment income that we are able to generate is affected by many factors, some of which are beyond our control. Some of these factors are volatility in the financial markets, economic growth, inflation, changes in interest rates, world political conditions, terrorist attacks or threats of terrorism, adverse events affecting other companies in our industry or the industries in which we invest and other unpredictable national or world events. Net investment income increased 3.3 percent in 2018, compared with the same period of 2017, primarily due to an increase in invested assets. The valuation of our investments in limited liability partnerships varies from period to period due to current equity market conditions. We expect to maintain our investment philosophy of purchasing quality investments rated investment grade or better.

We regularly monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires other-than-temporary impairment charges to be recorded when we determine that it is more likely than not that we will be unable to collect all amounts due according to the contractual terms of the fixed maturity security or that the anticipated recovery in fair value of the equity security will not occur in a reasonable amount of time. Impairment charges on investments are recorded based on the fair value of the investments at the measurement date or based on the value calculated using a discounted cash flow model. Factors considered in evaluating whether a decline in value is other-than-temporary include: the length of time and the extent to which fair value has been less than cost; the financial condition and near-term prospects of the issuer; our intention to hold the investment; and the likelihood that we will be required to sell the investment.

Changes in unrealized gains and losses on available-for-sale fixed-maturity securities do not affect net income and earnings per share but do impact comprehensive income, stockholders' equity and book value per share. We believe that any unrealized losses on our available-for-sale fixed-maturity securities at December 31, 2018 are temporary based upon our current analysis of the issuers of the securities that we hold and current market conditions. It is



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possible that we could recognize impairment charges in future periods on securities that we own at December 31, 2018 if future events and information cause us to determine that a decline in value is other-than-temporary. However, we endeavor to invest in high quality assets to provide protection from future credit quality issues and corresponding other-than-temporary impairment write-downs.

**Net Investment Income**

In 2018, our investment income for continuing operations, net of investment expenses, increased \$1.7 million to \$52.9 million as compared to 2017, primarily due to the increase in our invested assets in our portfolio partially offset by a decrease in the value of our investments in limited liability partnerships in the fourth quarter, specifically related to financial institutions.

In 2017, our investment income for continuing operations, net of investment expenses, decreased \$4.1 million to \$51.2 million as compared to 2016, primarily due to the change in value of our investments in limited liability partnerships, specifically related to financial institutions.

The following table summarizes the components of net investment income:

<i>(In Thousands)</i>	2018	2017	2016
Years Ended December 31,			
Investment income from continuing operations:			
Interest on fixed maturities	<b>\$51,356</b>	\$44,784	\$43,147
Dividends on equity securities	<b>7,731</b>	7,108	6,448
Income on other long-term investments			
Interest	<b>8,383</b>	6,870	1,200
Change in value <sup>(1)</sup>	<b>(10,116 )</b>	(2,812 )	10,178
Interest on mortgage loans	<b>412</b>	—	—
Interest on short-term investments	<b>606</b>	120	47
Interest on cash and cash equivalents	<b>1,875</b>	1,125	352
Other	<b>307</b>	300	422
Total investment income from continuing operations	<b>\$60,554</b>	\$57,495	\$61,794
Less investment expenses	<b>7,660</b>	6,305	6,510
Net investment income from continuing operations	<b>\$52,894</b>	\$51,190	\$55,284
Net investment income from discontinued operations	<b>12,663</b>	49,720	51,538
Net investment income	<b>\$65,557</b>	\$100,910	\$106,822

(1) Represents the change in value of our interests in limited liability partnerships that are recorded on the equity method of accounting.

In 2018, 84.8 percent of our gross investment income from continuing operations originated from interest on fixed maturities, compared to 77.9 percent and 69.8 percent in 2017 and 2016, respectively.

The following table details our annualized yield on average invested assets from continuing operations for 2018, and both continuing and discontinued operations for 2017 and 2016, which is based on our invested assets (including money market accounts) at the beginning and end of the year divided by net investment income:

*(In Thousands)*

Years ended December 31,	Average Invested Assets	Investment Income, Net	Annualized Yield on Average Invested Assets
<b>2018</b>	<b>\$1,986,239</b>	<b>\$ 52,894</b>	<b>2.7 %</b>
2017	3,333,809	100,910	3.0 %
2016	3,223,014	106,822	3.3 %



Table of Contents**Net Realized Investment Gains and Losses**

The following table summarizes the components of our net realized investment gains or losses:

<i>(In Thousands)</i>	2018	2017	2016
Years Ended December 31,			
Net realized investment gains (losses) from continuing operations:			
Fixed maturities:			
Available-for-sale	<b>\$(254 )</b>	\$829	\$1,004
Trading securities			
Change in fair value	<b>(296 )</b>	924	189
Sales	<b>1,226</b>	244	931
Equity securities	<b>(20,292 )</b>	1,942	2,654
Mortgage loans	<b>(46 )</b>	—	—
Cash equivalents	<b>—</b>	—	169
Real Estate	<b>(517 )</b>	116	\$—
Total net realized investment gains from continuing operations	<b>\$(20,179)</b>	\$4,055	\$4,947
Total net realized investment gains from discontinued operations	<b>(1,057 )</b>	4,008	1,156
Total net realized investment gains	<b>\$(21,236)</b>	\$8,063	\$6,103

**Net Unrealized Investment Gains and Losses**

As of December 31, 2018, net unrealized investment losses, after tax, totaled \$9.3 million compared to gains of \$214.9 million and \$133.9 million as of December 31, 2017 and 2016, respectively. The decrease in net unrealized investment gains in 2018 is primarily the result of the cumulative change in accounting principles on recognizing the change in the value of equity securities in the income statement. The change in accounting principles required unrealized gains on equity securities of \$191.2 million, after-tax, as of January 1, 2018, to be reclassified to retained earnings from accumulated other comprehensive income, both within shareholders equity. The remaining decrease is due to a decrease in the value of the fixed maturity portfolio due to rising interest rates.

The increase in net unrealized investment gains in 2017 is primarily the result of a decrease in interest rates, which positively impacted the valuation of our fixed maturity security portfolio during 2017 and an increase in the fair value of our equity security portfolio. Our net unrealized investment gains also increased due to the decrease in the tax rate from the Tax Act enactment.

The increase in unrealized gains in 2016 is the result of an increase in the fair value of the equity securities portfolio due to an increase in the financial markets, partially offset by a decline in the fair value of the fixed maturity portfolio due to an increase in interest rates.

The following table summarizes the change in our net unrealized investment gains (losses):

<i>(In Thousands)</i>	2018	2017	2016
Years Ended December 31,			
Changes in net unrealized investment gains (losses):			
Available-for-sale fixed maturity securities	<b>\$(57,475 )</b>	\$25,573	\$(21,271)
Equity securities	<b>—</b>	40,168	34,179
Deferred policy acquisition costs	<b>7,274</b>	119	(4,410 )
Income tax effect	<b>10,543</b>	(21,545 )	(2,975 )
Cumulative change in accounting principles	<b>(191,244 )</b>	—	—
Net unrealized investment depreciation of discontinued operations, sold	<b>6,714</b>	—	—
Accumulated effect of change in enacted tax rate	<b>—</b>	36,658	—
Total change in net unrealized investment gains (losses), net of tax	<b>\$(224,188)</b>	\$80,973	\$5,523

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**Market Risk**

Our Consolidated Balance Sheets include financial instruments whose fair values are subject to market risk. The active management of market risk is integral to our operations. Market risk is the potential for loss due to a decrease in the fair value of securities resulting from uncontrollable fluctuations, such as: interest rate risk, equity price risk, foreign exchange risk, credit risk, inflation, or geopolitical conditions. Our primary market risk exposures are: changes in interest rates, deterioration of credit quality in specific issuers, sectors or the economy as a whole, and an unforeseen decrease in the liquidity of securities we hold. We have no foreign exchange risk.

*Interest Rate Risk*

Interest rate risk is the price sensitivity of a fixed income maturity security or portfolio of securities to changes in level of interest rates. Generally, there is an inverse relationship between changes in interest rates and changes in the price of a fixed income/maturity security. Plainly stated, if interest rates go up (down), bond prices go down (up). A vast majority of our holdings are fixed income maturity and other interest rate sensitive securities that will decrease (increase) in value as interest rates increase (decrease). While it is generally our intent to hold our investments in fixed maturity securities to maturity, we have classified a majority of our fixed maturity portfolio as available-for-sale. Available-for-sale fixed income maturity securities are carried at fair value on the Consolidated Balance Sheets with unrealized gains or losses reported net of tax in Accumulated Other Comprehensive Income. A change in the prevailing interest rates generally translates into a change in the fair value of our fixed income/maturity securities, and by extension, our overall book value.

*Market Risk and Duration*

We analyze potential changes in the value of our investment portfolio due to the market risk factors noted above within the overall context of asset and liability management. A technique we use in the management of our investment portfolio is the calculation of duration. Our actuaries estimate the payout pattern of our reserve liabilities to determine their duration, which is the present value of the weighted average payments expressed in years. We then establish a target duration for our investment portfolio so that at any given time the estimated cash generated by the investment portfolio will closely match the estimated cash required for the payment of the related reserves. We structure the investment portfolio to meet the target duration to achieve the required cash flow, based on liquidity and market risk factors.

*Impact of Interest Rate Changes*

The amounts set forth in the following table detail the impact of hypothetical interest rate changes on the fair value of fixed maturity securities held at December 31, 2018. The sensitivity analysis measures the change in fair values arising from immediate changes in selected interest rate scenarios. We employed hypothetical parallel shifts in the yield curve of plus or minus 100 and 200 basis points in the simulations. Additionally, based upon the yield curve shifts, we employ estimates of prepayment speeds for mortgage-related products and the likelihood of call or put options being exercised within the simulations.

The selection of a 100-basis-point and 200-basis-point increase or decrease in interest rates should not be construed as a prediction by our management of future market events, but rather as an illustration of the potential impact of an event.

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December 31, 2018 (In Thousands)	-200 Basis Points	-100 Basis Points	Base Base	+100 Basis Points	+ 200 Basis Points
<b>AVAILABLE-FOR-SALE</b>					
Fixed maturities					
Bonds					
U.S. Treasury	\$28,090	\$27,750	\$27,418	\$27,094	\$26,778
U.S. government agency	224,062	220,559	214,682	201,550	185,313
States, municipalities and political subdivisions					
General obligations:					
Midwest	104,340	99,954	95,212	89,449	83,506
Northeast	41,050	39,394	37,655	35,475	33,098
South	125,470	119,983	113,911	106,458	98,759
West	120,490	114,351	107,841	100,485	93,092
Special revenue:					
Midwest	157,199	149,419	140,764	130,359	119,927
Northeast	70,919	66,600	61,948	56,682	51,513
South	269,980	253,918	235,809	215,031	195,048
West	162,212	153,106	142,920	131,193	119,821
Foreign bonds	10,061	9,885	9,716	9,552	9,395
Public utilities	61,771	58,837	56,059	53,427	50,951
Corporate bonds					
Energy	30,934	29,762	28,648	27,589	26,586
Industrials	57,092	55,036	53,085	51,228	49,466
Consumer goods and services	58,721	56,113	53,646	51,307	49,096
Health care	18,064	17,340	16,658	16,015	15,410
Technology, media and telecommunications	29,566	27,804	26,176	24,670	23,281
Financial services	86,825	83,015	79,349	75,738	72,255
Mortgage backed securities	7,923	7,705	7,424	7,090	6,749
Collateralized mortgage obligations					
Government national mortgage association	86,049	81,833	76,701	71,269	65,932
Federal home loan mortgage corporation	112,069	110,683	107,623	102,138	95,917
Federal national mortgage association	56,798	55,505	52,748	49,102	45,414
Asset-backed securities	3,496	3,496	3,495	3,495	3,494
<b>Total Available-For-Sale Fixed Maturities</b>	<b>\$1,923,181</b>	<b>\$1,842,048</b>	<b>\$1,749,488</b>	<b>\$1,636,396</b>	<b>\$1,520,801</b>
<b>TRADING</b>					
Fixed maturities					
Bonds					
Corporate bonds					
Industrials	\$401	\$399	\$397	\$395	\$393
Consumer goods and services	1,674	1,636	1,599	1,563	1,528
Health care	3,788	3,481	3,236	3,038	2,878
Financial services	2,284	2,257	2,231	2,206	2,182
Technology, media and telecommunications	3,938	3,438	3,028	2,692	2,413
Redeemable preferred stock	2,749	2,749	2,749	2,749	2,749
<b>Total Trading Fixed Maturities</b>	<b>\$14,834</b>	<b>\$13,960</b>	<b>\$13,240</b>	<b>\$12,643</b>	<b>\$12,143</b>
<b>Total Fixed Maturity Securities</b>	<b>\$1,938,015</b>	<b>\$1,856,008</b>	<b>\$1,762,728</b>	<b>\$1,649,039</b>	<b>\$1,532,944</b>

To the extent actual results differ from the assumptions utilized, our duration and interest rate measures could be significantly affected. As a result, these calculations may not fully capture the impact of nonparallel changes in the relationship between short-term and long-term interest rates.

***Equity Price Risk***

Equity price risk is the potential loss arising from changes in the fair value (i.e., market price) of equity securities held in our portfolio. Changes in the price of an equity security may be due to a change in the future earnings capacity or strategic outlook of the security issuer, and what investors are willing to pay for those future earnings and related strategy. The carrying values of our equity securities are based on quoted market prices, from an independent source, as of the balance sheet date. Market prices of equity securities, in general, are subject to



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fluctuations that could cause the amount to be realized upon the future sale of the securities to differ significantly from the current reported value. The fluctuations may result from perceived changes in the underlying economic characteristics of the security issuer, the relative price of alternative investments, general market conditions, and supply/demand factors related to a particular security.

*Impact of Price Change*

The following table details the effect on the fair value of our investments in equity securities for a positive and negative 10 percent price change at December 31, 2018:

<i>(In Thousands)</i>	-10%	Base	+10%
Estimated fair value of equity securities	\$223,525	\$248,361	\$273,197

**Foreign Currency Exchange Rate Risk**

Foreign currency exchange rate risk arises from the possibility that changes in foreign exchange rates will impact our transactions with foreign reinsurers relating to the settlement of amounts due to or from foreign reinsurers in the normal course of business. We consider this risk to be immaterial to our operations.

**Credit Risk**

Credit risk is the willingness and ability of a borrower to repay on time and in full any principal and interest due to the lender. Losses related to credit risk are realized through the income statement and have a direct impact on the earnings of UFG. Given the vast majority of our holdings are fixed income maturity securities, we view credit risk as our primary investment risk. Our internal Investment Department has developed and maintains a rigorous underwriting process to analyze and measure the expected frequency and severity of loss (i.e., credit quality) for government, agency, municipal, structured security, and corporate bond issuers. The objective is to maintain the appropriate balance of risk in our portfolio, consistent with our Investment Policy Statement and conservative investment style, and ensure the portfolio is compensated appropriately for the credit risk it holds. We do have within our municipal bond holdings a small number of securities whose ratings were enhanced by third-party insurance for the payment of principal and interest in the event of an issuer default. Of the insured municipal securities in our investment portfolio, 99.5 percent and 99.1 percent were rated "A" or above, and 94.7 percent and 93.7 percent were rated "AA" or above at December 31, 2018 and 2017, respectively, without the benefit of insurance. Due to the underlying financial strength of the issuers of the securities, we believe that the loss of insurance would not have a material impact on our operations, financial position, or liquidity.

We have no direct exposure in any of the guarantors of our investments. Our largest indirect exposure with a single guarantor totaled \$20.0 million or 19.5 percent of our insured municipal securities at December 31, 2018, as compared to \$20.0 million or 20.8 percent at December 31, 2017. Our five largest indirect exposures to financial guarantors accounted for 73.7 percent and 66.6 percent of our insured municipal securities at December 31, 2018 and 2017, respectively.

**LIQUIDITY AND CAPITAL RESOURCES**

Liquidity measures our ability to generate sufficient cash flows to meet our short- and long-term cash obligations. Our cash inflows are primarily a result of the receipt of premiums, reinsurance recoveries, sales or maturities of investments, and investment income. Cash provided from these sources is used to fund the payment of losses and loss settlement expenses, the purchase of investments, operating expenses, dividends, pension plan contributions, and in recent years, common stock repurchases.

We monitor our capital adequacy to support our business on a regular basis. The future capital requirements of our business will depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. Our ability to underwrite is largely dependent upon the quality of our claims paying and financial strength ratings as evaluated by independent rating agencies. In

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particular, we require (1) sufficient capital to maintain our financial strength ratings, as issued by various rating agencies, at a level considered necessary by management to enable our insurance company subsidiaries to compete and (2) sufficient capital to enable our insurance company subsidiaries to meet the capital adequacy tests performed by regulatory agencies in the United States.

Cash outflows may be variable because of the uncertainty regarding settlement dates for losses. In addition, the timing and amount of individual catastrophe losses are inherently unpredictable and could increase our liquidity requirements. The timing and amount of reinsurance recoveries may be affected by reinsurer solvency and reinsurance coverage disputes.

Historically, we have generated substantial cash inflows from operations. It is our policy to invest the cash generated from operations in securities with maturities that, in the aggregate, correlate to the anticipated timing of payments for losses and loss settlement expenses. The majority of our assets are invested in available-for-sale fixed maturity securities.

The following table displays a summary of cash sources and uses in 2018, 2017 and 2016 from continuing and discontinued operations:

Cash Flow Summary (In Thousands)	Years Ended December 31,		
	2018	2017	2016
Cash provided by (used in)			
Operating activities	\$110,104	\$170,094	\$214,384
Investing activities	(19,204 )	(61,985 )	(112,403 )
Financing activities	(115,188 )	(107,549 )	(97,577 )
Net increase (decrease) in cash and cash equivalents	\$(24,288 )	\$560	\$4,404

In the Consolidated Statement of Cash Flows, cash flows from discontinued operations are shown in separate lines in each of the operating, investing and financing sections of the Cash Flow Statement. Our cash flows from continuing operations were sufficient to meet our current liquidity needs for the full-year periods ended December 31, 2018, 2017 and 2016 and we anticipate they will be sufficient to meet our future liquidity needs.

**Operating Activities**

Net cash flows provided by operating activities totaled \$110.1 million, \$170.1 million and \$214.4 million in 2018, 2017 and 2016, respectively. Our cash flows from operations were sufficient to meet our liquidity needs for 2018, 2017 and 2016.

**Investing Activities**

Cash in excess of operating requirements is generally invested in fixed maturity securities and equity securities. Fixed maturity securities provide regular interest payments and allow us to match the duration of our liabilities. Equity securities provide dividend income, potential dividend income growth and potential appreciation. For further discussion of our investments, including our philosophy and portfolio, see the "Investment Portfolio" section contained in this Item.

In addition to investment income, possible sales of investments and proceeds from calls or maturities of fixed maturity securities also can provide liquidity. During the next five years, \$0.3 billion, or 15.8 percent of our fixed maturity portfolio will mature.

We invest funds required for short-term cash needs primarily in money market accounts, which are classified as cash equivalents. At December 31, 2018, our cash and cash equivalents included \$3.3 million related to these money market accounts, compared to \$16.8 million at December 31, 2017.

Net cash flows used in investing activities totaled \$19.2 million, \$62.0 million and \$112.4 million in 2018, 2017 and 2016, respectively. In 2018, we had cash inflows from scheduled and unscheduled investment maturities,

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redemptions, prepayments, and sales of investments, from continuing operations, that totaled \$263.8 million compared to \$205.1 million and \$328.1 million for the same period in 2017 and 2016, respectively. In 2018, we had cash inflows from scheduled and unscheduled investment maturities, redemptions, prepayments, and sales of investments, from discontinued operations, that totaled \$29.7 million compared to \$148.6 million and \$223.0 million for the same period in 2017 and 2016, respectively.

Our cash outflows for investment purchases from continuing operations totaled \$540.4 million in 2018, compared to \$267.5 million and \$448.2 million for the same period in 2017 and 2016, respectively. Our cash outflows for investment purchases from discontinued operations totaled \$15.4 million in 2018, compared to \$131.0 million and \$207.7 million for the same period in 2017 and 2016, respectively.

**Financing Activities**

Net cash flows used in financing activities totaled \$115.2 million, \$107.5 million and \$97.6 million in 2018, 2017 and 2016, respectively. Net cash flows used in financing activities from continuing operations totaled \$103.6 million, \$52.3 million and \$19.2 million in 2018, 2017 and 2016, respectively. The change is due to an increase in the payment of cash dividends partially offset by a decrease in the repurchases of common stock. Net cash flows used in financing activities from discontinued operations totaled \$11.5 million, \$55.3 million and \$78.3 million in 2018, 2017 and 2016, respectively, primarily due to net annuity withdrawals.

**Dividends**

Dividends paid to shareholders totaled \$105.4 million, \$27.3 million and \$24.6 million in 2018, 2017 and 2016, respectively. The increase in dividends paid to shareholders is primarily due to a special cash dividend of \$3.00 per share paid to shareholders on August 20, 2018. Our practice has been to pay quarterly cash dividends, which we have paid every quarter since March 1968.

Payments of any future dividends and the amounts of such dividends, however, will depend upon factors such as net income, financial condition, capital requirements, and general business conditions. We will only pay dividends if declared by our Board of Directors out of legally available funds.

As a holding company with no independent operations of its own, United Fire Group, Inc. relies on dividends received from its insurance company subsidiaries in order to pay dividends to its common shareholders. Dividends payable by our insurance subsidiaries are governed by the laws in the states in which they are domiciled. In all cases, these state laws permit the payment of dividends only from earned surplus arising from business operations. For example, under Iowa law, the maximum dividend or distribution that may be paid within a 12-month period without prior approval of the Iowa Insurance Commissioner is generally restricted to the greater of 10 percent of statutory surplus as of the preceding December 31, or net income of the preceding calendar year on a statutory basis, not greater than earned statutory surplus. Other states in which our insurance company subsidiaries are domiciled may impose similar restrictions on dividends and distributions. Based on these restrictions, at December 31, 2018, our insurance company subsidiary, United Fire & Casualty, is able to make a minimum of \$106.2 million in dividend payments without prior regulatory approval. These restrictions are not expected to have a material impact in meeting our cash obligations. On June 20, 2018, the Company sought approval from the Iowa Insurance Commissioner for a proposed ordinary dividend of \$50.7 million and extraordinary dividend of \$39.3 million, for a total of \$90.0 million. The Company received approval from Iowa Insurance Commissioner on July 9, 2018 and subsequently paid a \$3.00 per share special dividend or a total of \$75.2 million to shareholders on August 20, 2018.

**Share Repurchases**

Under our share repurchase program, first announced in August 2007, we may purchase our common stock from time to time on the open market or through privately negotiated transactions. The amount and timing of any purchases will be at our discretion and will depend upon a number of factors, including the share price, economic and general market conditions, and corporate and regulatory requirements. Our share repurchase program may be modified or discontinued at any time.

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During 2018, 2017 and 2016, pursuant to authorization by our Board of Directors, we repurchased 120,372, 701,899, and 90,415 shares of our common stock, respectively, which used cash totaling \$5.4 million in 2018, \$29.8 million in 2017 and \$3.7 million in 2016. At December 31, 2018, we were authorized to purchase an additional 2,116,200 shares of our common stock under our share repurchase program, which expires in August 2020.

**Credit Facilities**

Information specific to our credit facilities is incorporated by reference from Note 14 "Credit Facility" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**Stockholders' Equity**

Stockholders' equity decreased 8.7 percent to \$888.4 million at December 31, 2018, from \$973.4 million at December 31, 2017. The decrease is primarily attributed to the payment of stockholder dividends of \$105.4 million, and a decrease in net unrealized investment gains of \$32.9 million, net of tax, and share repurchases of \$5.4 million, all offset by net income of \$27.7 million and the change in benefits and the valuation of our post-retirement benefit obligations of \$25.4 million. As of December 31, 2018, the book value per share of our common stock was \$35.40, compared to \$39.06 at December 31, 2017.

**Risk-Based Capital**

The NAIC adopted risk-based capital requirements, which requires us to calculate a minimum capital requirement for each of our insurance companies based on individual company insurance risk factors. These "risk-based capital" results are used by state insurance regulators to identify companies that require regulatory attention or the initiation of regulatory action. At December 31, 2018, all of our insurance companies had capital well in excess of required levels.

**Contractual Obligations and Commitments**

The following table shows our contractual obligations and commitments, including our estimated payments due by period at December 31, 2018:

(In Thousands)

Contractual Obligations	Payments Due By Period				
	Total	Less Than One Year	One to Three Years	Three to Five Years	More Than Five Years
Loss and loss settlement expense reserves	1,312,483	480,834	448,945	171,220	211,484
Operating leases	21,682	7,214	11,527	2,760	181
Profit-sharing commissions	21,350	21,350			
Pension plan contributions	4,000	4,000			
Total	\$1,359,515	\$513,398	\$460,472	\$173,980	\$211,665

**Loss and Loss Settlement Expense Reserves**

The amounts presented are estimates of the dollar amounts and time periods in which we expect to pay out our gross loss and loss settlement expense reserves. Because the timing of future payments may vary from the stated contractual obligation, these amounts are estimates based upon historical payment patterns and may not represent actual future payments. Refer to "Critical Accounting Policies — Loss and Loss Settlement Expenses" in this section for further discussion.

**Operating Leases**

Our operating lease obligations are for the rental of office space, vehicles, computer equipment and office equipment. For further discussion of our operating leases, refer to Part II, Item 8, Note 13 "Lease Commitments."

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***Profit-Sharing Commissions***

We offer our agents a profit-sharing plan as an incentive for them to place high-quality property and casualty insurance business with us. Based on business produced by the agencies in 2018, property and casualty agencies will receive profit-sharing payments of \$21.4 million in 2019.

***Pension Plan Payments***

We estimate the pension contribution for 2019 in accordance with the Pension Protection Act of 2006 (the "Act"). Contributions for future years are dependent on a number of factors, including actual performance versus assumptions made at the time of the actuarial valuations and maintaining certain funding levels relative to regulatory requirements. Contributions in 2019, and in future years, are expected to be at least equal to the IRS minimum required contribution in accordance with the Act.

**OFF BALANCE SHEET ARRANGEMENTS**

**Funding Commitments**

We hold investments in limited liability partnerships as part of our investment strategy. At December 31, 2018, pursuant to an agreement with our limited liability partnership investments, we are contractually committed to make consolidated capital contributions up to \$22.3 million upon request of the partnerships through July 31, 2028. These partnerships are included in our other invested assets on the Consolidated Balance Sheets with a current fair value of \$8.8 million, or less than 0.5% of our total invested assets, at December 31, 2018. We recognized investment income of \$0.5 million from these two investments during 2018.

**CRITICAL ACCOUNTING POLICIES**

Critical accounting policies are defined as those that are representative of significant judgments and uncertainties and that may potentially result in materially different results under different assumptions and conditions. We base our discussion and analysis of our results of operations and financial condition on the amounts reported in our Consolidated Financial Statements, which we have prepared in accordance with GAAP. As we prepare these Consolidated Financial Statements, we must make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses for the reporting period. We evaluate our estimates on an ongoing basis. We base our estimates on historical experience and on other assumptions we believe to be reasonable under the circumstances. Actual results could differ from those estimates. We believe our most critical accounting policies are as follows.

**Investment Valuation**

Upon acquisition, we classify investments in marketable securities as held-to-maturity, available-for-sale, or trading. We record investments in held-to-maturity fixed maturity securities at amortized cost. We record investments in available-for-sale and trading fixed maturity securities and equity securities at fair value. Other long-term investments consist primarily of our interests in limited liability partnerships that are recorded on the equity method of accounting. We record mortgage loans at their amortized cost less any valuation allowance.

In general, investment securities are exposed to various risks, such as interest rate risk, credit risk, and overall market volatility risk. Therefore, it is reasonably possible that changes in the fair value of our investment securities that are reported at fair value will occur in the near term and such changes could materially affect the amounts reported in the Consolidated Financial Statements. Also, it is reasonably possible that changes in the value of our investments in trading securities and limited liability partnerships could occur in the future and such changes could materially affect our results of operations as reported in our Consolidated Financial Statements.

Table of Contents***Fair Value Measurement***

Information specific to the fair value measurement of our financial instruments and disclosures is incorporated by reference from Note 3 "Fair Value of Financial Instruments" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

***Other-Than-Temporary Impairment ("OTTI") Charges***

We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires OTTI charges to be recorded when we determine that it is more likely than not that we will be unable to collect all amounts due according to the contractual terms of the fixed maturity security. Impairment charges on investments are recorded based on the fair value of the investments at the measurement date or based on the value calculated using a discounted cash flow model. Factors considered in evaluating whether a decline in value is other-than-temporary include: the length of time and the extent to which fair value has been less than cost; the financial condition and near-term prospects of the issuer; our intention to hold the investment; and the likelihood that we will be required to sell the investment.

The determination of the amount of impairments varies by investment type and is based upon our periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available. Additionally, our management considers a wide range of factors about the instrument issuer and uses its best judgment in evaluating the cause of the decline in the estimated fair value of the instrument and in assessing the prospects for recovery. Inherent in management's evaluation of the security are assumptions and estimates about the operations of the issuer and its future earnings potential.

At December 31, 2018 and 2017, we had a number of securities with fair value less than the cost basis. The total unrealized loss on these securities was \$23.6 million at December 31, 2018, compared with \$16.9 million at December 31, 2017. Our rationale for not recording OTTI charges on these securities is discussed in Part II, Item 8, Note 2 "Summary of Investments."

***Deferred Policy Acquisition Costs ("DAC")***

We record an asset for certain costs of underwriting new business, primarily commissions, premium taxes and variable underwriting and policy issue expenses that have been deferred. The amount of underwriting compensation expense eligible for deferral is based on time studies and a ratio of success in policy placement. At December 31, 2018 and 2017, our DAC asset was \$92.8 million and \$88.1 million, respectively.

The DAC asset is amortized over the life of the policies written, generally one year. We assess the recoverability of DAC on a quarterly basis by line of business. This assessment is performed by comparing recorded unearned premium to the sum of unamortized DAC and estimates of expected losses and loss settlement expenses. If the sum of these costs exceeds the amount of recorded unearned premium (i.e., the line of business is expected to generate an operating loss), the excess is recognized in current period other underwriting expenses as an offset against the established DAC asset. We refer to this offset as a premium deficiency charge.

To calculate the premium deficiency charge by line of business, we estimate an expected loss and loss settlement expense ratio which is based on our best estimate of future losses for each line of business. This calculation is performed on a quarterly basis and developed in conjunction with our quarterly reserving process. The expected loss and loss settlement expense ratios are the only assumptions we utilize in our premium deficiency calculation. Changes in these assumptions can have a significant impact on the amount of premium deficiency charge recognized for a line of business. The premium deficiency calculation is aggregated by line of business in a manner consistent with how the policies are currently being marketed and managed.

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The following table illustrates the hypothetical impact on the premium deficiency charge recorded for the quarter ended December 31, 2018, of reasonably likely changes in the assumed loss and loss settlement expense ratios utilized for purposes of this calculation. The entire impact of these changes would be recognized through income as other underwriting expenses. The following table illustrates the impact of potential changes in the expected loss and loss settlement expense ratios for all lines of business on the premium deficiency charge. The base amount indicated below is the actual premium deficiency charge recorded as an offset against the DAC asset established as of the quarter ended December 31, 2018:

Sensitivity Analysis — Impact of Changes in Projected Loss and Loss

Settlement Expense Ratios

(In Thousands)	-10%	-5%	Base	+5%	+10%
Premium deficiency charge estimated \$	—\$	—\$4,341	\$12,964	\$23,691	

Actual future results could differ materially from our assumptions used to calculate the recorded DAC asset. Changes in our assumed loss and loss settlement expense ratios in the future would impact the amount of deferred costs in the period such changes in assumptions are made. The premium deficiency charge calculated for the quarter ended December 31, 2018 was \$4.3 million compared to the premium deficiency charge of \$6.1 million calculated for the same period of 2017.

**Losses and Loss Settlement Expenses**

Reserves for losses and loss settlement expenses are reported using our best estimate of ultimate liability for claims that occurred prior to the end of any given reporting period, but have not yet been paid. Before credit for reinsurance recoverables, these reserves were \$1,312.5 million and \$1,224.2 million at December 31, 2018 and 2017, respectively. We purchase reinsurance to mitigate the impact of large losses and catastrophic events. Loss and loss settlement expense reserves ceded to reinsurers were \$57.1 million for 2018 and \$59.9 million for 2017. Our reserves, before credit for reinsurance recoverables, by line of business as of December 31, 2018, were as follows:

(In Thousands)	Case Basis	IBNR	Loss Settlement Expense	Total Reserves
<b>Commercial lines</b>				
Fire and allied lines	\$81,463	\$10,470	\$22,756	\$114,689
Other liability	267,270	108,220	174,344	549,834
Automobile	229,405	66,470	75,696	371,571
Workers' compensation	176,467	5,000	29,269	210,736
Fidelity and surety	4,127	2,520	399	7,046
Miscellaneous	505	520	158	1,183
Total commercial lines	\$759,237	\$193,200	\$302,622	\$1,255,059
<b>Personal lines</b>				
Automobile	\$12,453	\$1,070	\$2,407	\$15,930
Fire and allied lines	9,205	1,080	2,194	12,479
Miscellaneous	448	190	162	800
Total personal lines	\$22,106	\$2,340	\$4,763	\$29,209
Reinsurance assumed	9,525	18,560	130	28,215
Total	\$790,868	\$214,100	\$307,515	\$1,312,483

**Case-Basis Reserves**

For each of our lines of business, with respect to reported claims, we establish reserves on a case-by-case basis. Our experienced claims personnel estimate these case-basis reserves using adjusting guidelines established by management. Our goal is to set the case-basis reserves at the ultimate expected loss amount as soon as possible after information about the claim becomes available.





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Establishing the case reserve for an individual claim is subjective and complex, requiring us to estimate future payments and values that will be sufficient to settle an individual claim. Setting a reserve for an individual claim is an inherently uncertain process. When we establish and adjust individual claim reserves, we do so based on our knowledge of the circumstances and facts of the claim. Upon notice of a claim, we establish a preliminary (average claim cost) reserve based on the limited claim information initially reported. Subsequently, we conduct an investigation of each reported claim, which allows us to more fully understand the factors contributing to the loss and our potential exposure. This investigation may extend over a long period of time. As our claim investigation progresses, and as our claims personnel identify trends in claims activity, we may refine and adjust our estimates of case reserves. To evaluate and refine our overall reserving process, we track and monitor all claims until they are settled and paid in full, with all salvage and subrogation claims being resolved.

Most of our insurance policies are written on an occurrence basis that provides coverage if a loss occurs during the policy period, even if the insured reports the loss many years later. For example, some liability claims for construction defect coverage are reported 10 years or more after the policy period, and the workers' compensation coverage provided by our policies pays unlimited medical benefits for the duration of the claimant's injury up to the lifetime of the claimant. In addition, final settlement of certain claims can be delayed for years due to litigation or other reasons. Reserves for these claims require us to estimate future costs, including the effect of judicial actions, litigation trends and medical cost inflation, among others. Reserve development can occur over time as conditions and circumstances change many years after the policy was issued and/or the loss occurred.

Our loss reserves include amounts related to both short-tail and long-tail lines of business. "Tail" refers to the time period between the occurrence of a loss and the ultimate settlement of the claim. A short-tail insurance product is one where ultimate losses are known and settled comparatively quickly. Ultimate losses under a long-tail insurance product are sometimes not known and settled for many years. The longer the time span between the incidence of a loss and the settlement of the claim, the more the ultimate settlement amount can vary from the reserves initially established. Accordingly, long-tail insurance products can have significant implications on the reserving process. Our short-tail lines of business include fire and allied lines, homeowners, commercial property, auto physical damage and inland marine. The amounts of the case-based reserves that we establish for claims in these lines depend upon various factors, such as individual claim facts (including type of coverage and severity of loss), our historical loss experience and trends in general economic conditions (including changes in replacement costs, medical costs and inflation).

For short-tail lines of business, the estimation of case-basis loss reserves is less complex than for long-tail lines because the claims relate to tangible property. Because of the relatively short time from claim occurrence to settlement, actual losses typically do not vary significantly from reserve estimates.

Our long-tail lines of business include workers' compensation and other liability. In addition, certain product lines such as personal and commercial auto, commercial multi-peril and surety include both long-tail coverages and short-tail coverages. For many long-tail liability claims, significant periods of time, ranging up to several years, may elapse between the occurrence of the loss, the reporting of the loss to us and the settlement of the claim. As a result, loss experience in the more recent accident years for the long-tail liability coverages has limited statistical credibility in our reserving process because a relatively small proportion of losses in these accident years are reported claims and an even smaller proportion are paid losses. In addition, long-tail liability claims are more susceptible to litigation and can be significantly affected by changing contract interpretations and the legal environment. Consequently, the estimation of loss reserves for long-tail coverages is more complex and subject to a higher degree of variability than for short-tail coverages.

The amounts of the case-basis loss reserves that we establish for claims in long-tail lines of business depends upon various factors, including individual claim facts (including type of coverage, severity of loss and underlying policy limits), company historical loss experience, changes in underwriting practice, legislative enactments, judicial decisions, legal developments in the awarding of damages, changes in political attitudes and trends in general economic conditions, including inflation. As with our short-tail lines of business, we review and make changes to long-tail case-based reserves based on our review of continually evolving facts as they become available to us



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during the claims settlement process. Our adjustments to case-based reserves are reported in the financial statements in the period that new information arises about the claim. Examples of facts that become known that could cause us to change our case-based reserves include, but are not limited to: evidence that loss severity is different than previously assessed; new claimants who have presented claims; and the assessment that no coverage exists.

***Incurred But Not Reported Reserves***

On a quarterly basis, the Company's internal actuary performs a detailed analysis of IBNR reserves. This analysis uses various loss projection methods to provide several estimates of ultimate loss (or loss adjustment expense ("LAE")) for each individual year and line of business. The loss projection methods include paid loss development; reported loss development; expected loss emergence based on paid losses; and expected loss emergence based on reported losses. The two methods utilized by our internal actuary to project loss settlement expenses are paid expenses development and development of the ratio of paid expense versus paid loss. Results of the projection methods are compared and a point estimate of ultimate loss (or LAE) is established for each individual year and line of business. The specific projection methods used to establish point estimates vary depending on what is deemed most appropriate for a particular line of business and year. Results of these methods are usually averaged together to provide a final point estimate. Given that there are several inputs depending on the line of business, the methods may be averaged and modified based on changes known to management or trends in the market. IBNR estimates are derived by subtracting reported loss from the final point estimate loss.

Senior management meets with our internal actuary and controller quarterly to review the adequacy of carried IBNR reserves based on results from this actuarial analysis and makes adjustments for changes in business and other factors not completely captured by the data within the actuarial analysis. There are two fundamental types or sources of IBNR reserves. We record IBNR for "normal" types of claims and also specific IBNR reserves related to unique circumstances or events. A major hurricane is an example of an event that might necessitate specific IBNR reserves because an analysis of existing historical data would not provide an appropriate estimate. This method of establishing our IBNR reserves has consistently resulted in aggregate reserve levels that management believes are reasonable in comparison to the reserve estimates indicated by the actuarial analysis.

For our short-tail lines of business, IBNR reserves constitute a small portion of the overall reserves. These claims are generally reported and settled shortly after the loss occurs. In our long-tail lines of business, IBNR reserves constitute a relatively higher proportion of total reserves, because, for many liability claims, significant periods of time may elapse between the initial occurrence of the loss, the reporting of the loss to us, and the ultimate settlement of the claim.

***Loss Settlement Expense Reserves***

Loss settlement expense reserves include amounts ultimately allocable to individual claims, as well as amounts required for the general overhead of the claims handling operation that are not specifically allocable to individual claims. We do not establish loss settlement expense reserves on a claim-by-claim basis. Instead, on a quarterly basis, our internal actuary performs a detailed statistical analysis (using historical data) to estimate the required reserve for unpaid loss settlement expenses. On a monthly basis, the required reserve estimate is adjusted to reflect additional earned exposure and expense payments that have occurred subsequent to completion of the quarterly analysis. LAE is composed of two distinct kinds of expenses which are allocated LAE ("ALAE") and unallocated LAE ("ULAE"). These two expense types have different purposes and characteristics which necessitates different estimation methods in order to provide a valid quarterly estimate of the required reserve for unpaid expense which is generally referred to as an LAE IBNR reserve.

Reserves for unpaid ALAE are estimated quarterly by line of business for each individual accident year using three methods: (1) Paid development, (2) Expected emergence of ALAE, and (3) Development of the ratio of paid ALAE to paid loss. Each of the three methods produces an estimate of the ultimate ALAE cost for an individual accident year and the final estimate is generally a weighted average of the various methods. Inception to date paid ALAE is

subtracted from the final ultimate ALAE estimate to provide the estimated ALAE IBNR reserve for each individual accident year.

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Reserves for unpaid ULAE are estimated quarterly by line of business for each individual accident year using a single method. This method consists of applying a percentage factor to unpaid loss reserves. The percentage factor used differs by line of business and is evaluated and established on an annual basis using year-end data. The percentage factor is evaluated and selected after reviewing the ratio of paid ULAE to paid loss using calendar year data for the most recent five years.

Generally, the loss settlement expense reserves for long-tail lines of business are a greater portion of the overall reserves, as there are often substantial legal fees and other costs associated with the complex liability claims that are associated with long-tail coverages. Because short-tail lines of business settle much more quickly and the costs are easier to determine, loss settlement expense reserves for such claims constitute a smaller portion of the total reserves.

***Reinsurance Reserves***

The estimation of assumed and ceded reinsurance loss and loss settlement expense reserves is subject to the same factors as the estimation of loss and loss settlement expense reserves. In addition to those factors, which give rise to inherent uncertainties in establishing loss and loss settlement expense reserves, there exists a delay in our receipt of reported claims for assumed business due to the procedure of having claims first reported through one or more intermediary insurers or reinsurers.

Reserves for assumed reinsurance are established using methods and techniques identical to those used for direct lines of business. The additional delay inherent in assumed reinsurance reporting is considered in our reserving process and payment is not problematic. Assumed reinsurance, like every independent line of business, has unique reporting and payment patterns that are reviewed as part of the reserve estimation process.

There are three distinct types of reserves ceded to reinsurers: (1) reported claim reserves, (2) loss IBNR, and (3) LAE IBNR. Ceded reserves for reported claims are calculated by subtracting the primary retention from the claim value established by our claim adjuster. Ceded loss IBNR originates solely from our boiler and machinery business which is 100 percent reinsured. For this business ceded loss IBNR is equal to direct loss IBNR. Boiler and machinery business is included in our commercial fire and allied line of business. We will cede some LAE expenses when we cede loss. Our ceded LAE IBNR is estimated based on our ceded unpaid loss reserves and the general relation, by line of business, between LAE and loss. Our primary retention was \$2.0 million for 2012 through 2015 and increased to \$2.5 million for 2016 through 2018.

***Key Assumptions***

Our internal and external actuaries and management use a number of key assumptions in establishing an estimate of loss and loss settlement expense reserves, including the following assumptions: future loss settlement expenses can be estimated based on the Company's historical ratios of loss settlement expenses paid to losses; the Company's case-basis reserves reflect the most up-to-date information available about the unique circumstances of each individual claim; no new judicial decisions or regulatory actions will increase our case-basis obligations; historical aggregate claim reporting and payment patterns will continue into the future consistent with the observable past; significant unique and unusual claim events have been identified and appropriate adjustments have been made; and, to the best of our knowledge, there are no new latent trends that would impact our case-basis reserves.

Our key assumptions are subject to change as actual claims occur and as we gain additional information about the variables that underlie our assumptions. Accordingly, management reviews and updates these assumptions periodically to ensure that the assumptions continue to be valid. If necessary, management makes changes not only in the estimates derived from the use of these assumptions, but also in the assumptions themselves. Due to the inherent uncertainty in the loss reserving process, management believes that there is a reasonable chance that modification to key assumptions could individually, or in aggregate, result in reserve levels that are either significantly above or below the actual amount for which the related claims will eventually settle.



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As an example, if our loss and loss settlement expense reserves of \$1,312.5 million as of December 31, 2018, is 10.0 percent inadequate, we would experience a reduction in future pre-tax earnings of up to \$131.2 million. This reduction could be recorded in one year or multiple years, depending on when we identify the deficiency. The deficiency would also affect our financial position in that our equity would be reduced by an amount equivalent to the reduction in net income. Any deficiency that would be recognized in our loss and loss settlement expense reserves usually does not have a material effect on our liquidity because the claims have not been paid. Conversely, if our estimates of ultimate unpaid loss and loss settlement expense reserves prove to be redundant, our future earnings and financial position would be improved. We believe our reserving philosophy, coupled with what we believe to be aggressive and successful claims management and loss settlement practices, has resulted in year-to-year redundancies in reserves. We believe our approach produces recorded reserves that are reasonable as to their relative position within a range of reasonable reserves from year-to-year.

We are unable to reasonably quantify the impact of changes in our key assumptions utilized to establish individual case-basis reserves on our total reported reserves because the impact of these changes would be unique to each specific case-basis reserve established. However, based on historical experience, we believe that aggregate case-basis reserve volatility levels of 5.0 percent and 10.0 percent can be attributed to the ultimate development of our net case-basis reserves. The impact to pre-tax earnings would be a decrease if the reserves were to be adjusted upwards and an increase if the reserves were to be adjusted downwards. The table below details the impact of this development volatility on our reported net case-basis reserves at December 31, 2018:

*(In Thousands)*

<b>Change in level of net case-basis reserve development</b>	5%	10%
Impact on reported net case-basis reserves	\$36,956	\$73,912

Due to the formula-based nature of our IBNR and loss settlement expense reserve calculations, changes in the key assumptions utilized to generate these reserves can impact our reported results. It is not possible to isolate and measure the potential impact of just one of these factors, and future loss trends could be partially impacted by all factors concurrently. Nevertheless, it is meaningful to view the sensitivity of the reserves to potential changes in these variables. To demonstrate the sensitivity of reserves to changes in significant assumptions, the following example is presented. The amounts reflect the pre-tax impact on earnings from a hypothetical percentage change in the calculation of IBNR and loss settlement expense reserves at December 31, 2018. The impact to pre-tax earnings would be a decrease if the reserves were to be adjusted upwards and an increase if the reserves were to be adjusted downwards. We believe that the changes presented are reasonably likely based upon an analysis of our historical IBNR and loss settlement expense reserve experience.

*(In Thousands)*

<b>Change in claim frequency and claim severity assumptions</b>	5%	10%
Impact due to change in IBNR reserving assumptions	\$10,682	\$21,364

*(In Thousands)*

<b>Change in LAE paid to losses paid ratio</b>	1%	2%
Impact due to change in LAE reserving assumptions	\$3,026	\$6,053

In 2018, we did not change the key method through which we develop our assumptions on which we based our reserving calculations. In estimating our 2018 loss and loss settlement expense reserves, we did not anticipate future events or conditions that were inconsistent with past development patterns.

Certain of our lines of business are subject to the potential for greater loss and loss settlement expense development than others, which are discussed below:





Table of Contents***Other Liability Reserves***

Other liability is considered a long-tail line of business, as it can take a relatively long period of time to settle claims from prior accident years. This is partly due to the lag time between the date a loss or event occurs that triggers coverage and the date when the claim is actually reported. Defense costs are also a part of the insured expenses covered by liability policies and can be significant, sometimes greater than the cost of the actual paid claims. For the majority of our products, defense costs are outside of the policy limit, meaning that the amounts paid for defense costs are not subtracted from the available policy limit.

Factors that can cause reserve uncertainty in estimating reserves in this line include: reporting time lags; the number of parties involved in the underlying tort action; whether the "event" triggering coverage is confined to only one time period or is spread over multiple time periods; the potential dollars involved in the individual claim actions; whether such claims were reasonably foreseeable and intended to be covered at the time the contracts were written (i.e., coverage disputes); and the potential for mass claim actions.

Claims with longer reporting time lags may result in greater inherent risk. This is especially true for alleged claims with a latency feature, particularly where courts have ruled that coverage is spread over multiple policy years, hence involving multiple defendants (and their insurers and reinsurers) and multiple policies (thereby increasing the potential dollars involved and the underlying settlement complexity). Claims with long latencies also increase the potential time lag between writing a policy in a certain market and the recognition that such policy has potential mass tort and/or latent claim exposure.

Our reserve for other liability claims at December 31, 2018, was \$549.8 million and consisted of 6,542 claims, compared with \$497.1 million, consisting of 6,336 claims at December 31, 2017. Of the \$549.8 million total reserve for other liability claims, \$143.4 million is identified as defense costs and \$31.0 million is identified as general overhead required in the settlement of claims.

Included in the other liability line of business are gross reserves for construction defect losses and loss settlement expenses. Construction defect is a liability allegation relating to defective work performed in the construction of structures such as commercial buildings, apartments, condominiums, single family dwellings or other housing, as well as the sale of defective building materials. These claims seek recovery due to damage caused by alleged deficient construction techniques or workmanship. At December 31, 2018, we had \$44.5 million in construction defect loss and loss settlement expense reserves, excluding IBNR reserves that are calculated for the overall other liability commercial line, which consisted of 2,706 claims. At December 31, 2017, our reserves, excluding IBNR reserves, totaled \$34.4 million, which consisted of 1,857 claims. The reporting of such claims can be delayed, as the statute of limitations can be up to 10 years. Court decisions in recent years have expanded insurers' exposure to construction defect claims. As a result, claims may be reported more than 10 years after a project has been completed, as litigation can proceed for several years before an insurance company is identified as a potential contributor. Claims have also emerged from parties claiming additional insured status on policies issued to other parties, such as contractors seeking coverage from a subcontractor's policy.

In addition to these issues, other variables also contribute to a high degree of uncertainty in establishing reserves for construction defect claims. These variables include: whether coverage exists; when losses occur; the size of each loss; expectations for future interpretive rulings concerning contract provisions; and the extent to which the assertion of these claims will expand geographically. In recent years, we have implemented various underwriting measures that we anticipate will mitigate the amount of construction defect losses experienced. These initiatives include increased care regarding additional insured endorsements; stricter underwriting guidelines on the writing of residential contractors; and an increased utilization of loss control.

***Asbestos and Environmental Reserves***

Included in the other liability and assumed reinsurance lines of business are reserves for asbestos and other environmental losses and loss settlement expenses. At December 31, 2018 and 2017, we had \$3.0 million and \$2.6 million, respectively, in direct and assumed asbestos and environmental loss reserves. The estimation of loss reserves for environmental claims and claims related to long-term exposure to asbestos and other substances is one



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of the most difficult aspects of establishing reserves, especially given the inherent uncertainties surrounding such claims. Although we record our best estimate of loss and loss settlement expense reserves, the ultimate amounts paid upon settlement of such claims may be more or less than the amount of the reserves, because of the significant uncertainties involved and the likelihood that these uncertainties will not be resolved for many years.

***Commercial Auto Reserves***

Commercial auto claim reserves are established at exposure based on information either known and provided or obtained through the investigation, with some pessimism built in. Incorporated are the perspective and experience the claims staff has acquired, which may include assumptions as to how the claim will develop over time, and with a slightly pessimistic view. Exposures are identified and reserves established within 30 to 60 days depending on the complexity of the case.

***Workers' Compensation Reserves***

Like the other liability line of business, workers' compensation losses and loss settlement expense reserves are based upon variables that create imprecision in estimating the ultimate reserve. Estimates for workers' compensation are particularly sensitive to assumptions about medical cost inflation, which has been steadily increasing over the past few years. Other variables that we consider and that contribute to the uncertainty in establishing reserves for workers' compensation claims include: state legislative and regulatory environments; trends in jury awards; and mortality rates. Because of these variables, the process of reserving for the ultimate loss and loss settlement expense to be incurred requires the use of informed judgment and is inherently uncertain. Consequently, actual loss and loss settlement expense reserves may deviate from our estimates. Such deviations may be significant. Our reserve for workers' compensation claims at December 31, 2018 was \$210.7 million and consisted of 4,337 claims, compared with \$211.3 million, consisting of 4,844 claims, at December 31, 2017.

***Reserve Development***

The following reserve development section should be read in conjunction with the "Consolidated Results of Operations" section of this Item 7.

In 2018, 2017 and 2016, we recognized a favorable development in our net reserves for prior accident years totaling \$54.2 million, \$54.3 million and \$31.2 million, respectively.

The factors contributing to our year-to-year redundancy include: establishing reserves at their ultimate expected loss amount as soon as practicable after information becomes available, which produces, on average, prudently conservative case reserves; using claims negotiation to control the size of settlements; assuming that we have liability for all claims, even though the issue of liability may, in some cases, be resolved in our favor; promoting claims management services to encourage return-to-work programs; case management by nurses for serious injuries and management of medical provider services and billings; and using programs and services to help prevent fraud and to assist in favorably resolving cases.

Based upon our comparison of carried reserves to actual claims experience over the last several years, we believe that using our Company's historical premium and claims data to establish reserves for losses and loss settlement expenses results in adequate and reasonable reserves. Reserve development is discussed in more detail under the heading "Reserve Development" in the "Consolidated Results of Operations" section in this Item.

The following table details the pre-tax impact on our property and casualty insurance business' financial results and financial condition of reasonably likely reserve development. Our lines of business that have historically been most susceptible to significant volatility in reserve development have been shown separately and utilize hypothetical levels of volatility of 5.0 percent and 10.0 percent. Our other, less volatile, lines of business have been aggregated and utilize hypothetical levels of volatility of 3.0 percent and 5.0 percent.

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<b>Hypothetical Reserve Development Volatility Levels</b>	<b>-10%</b>	<b>-5%</b>	<b>+5%</b>	<b>+10%</b>
Impact on loss and loss settlement expenses				
Other liability	\$(54,983)	\$(27,492)	\$27,492	\$54,983
Workers' compensation	(21,074 )	(10,537 )	10,537	21,074
Automobile	(38,750 )	(19,375 )	19,375	38,750

<b>Hypothetical Reserve Development Volatility Levels</b>	<b>-5%</b>	<b>-3%</b>	<b>+3%</b>	<b>+5%</b>
Impact on loss and loss settlement expenses				
All other lines	\$(8,221 )	\$(4,932 )	\$4,932	\$8,221

**Independent Actuary**

We engage an independent actuarial firm to render an opinion as to the reasonableness of the statutory reserves internal management establishes. During 2018 and 2017, we engaged the services of Regnier as our independent actuarial firm for the property and casualty insurance business. We anticipate that this engagement will continue in 2019.

It is management's policy to utilize staff adjusters to develop our estimate of case-basis loss reserves. IBNR and loss settlement expense reserves are established through various formulae that utilize pertinent, recent Company historical data. The calculations are supplemented with knowledge of current trends and events that could result in adjustments to the level of IBNR and loss settlement expense reserves. On a quarterly basis, we compare our estimate of total reserves to the estimates prepared by Regnier by line of business to ensure that our estimates are within the actuary's acceptable range. Regnier performs a review of loss and loss settlement expense reserves at each year end using generally accepted actuarial guidelines to ensure that the recorded reserves appear reasonable. Our net reserves for losses and loss settlement expenses as of December 31, 2018 and 2017 were \$1,255.4 million and \$1,164.3 million, respectively. In 2018 and 2017, after considering the independent actuary's range of reasonable estimates, management believes that carried reserves were reasonable and therefore did not adjust the recorded amount. Regnier uses four projection methods in its actuarial analysis of our loss reserves and uses two projection methods in its actuarial analysis of our loss settlement expense reserves. Based on the results of the projection methods, the actuaries select an actuarial point estimate of the reserves, which is compared to our carried reserves to evaluate the reasonableness of the carried reserves. The four methods utilized by Regnier to project losses are: paid loss development; reported loss development; expected loss emergence based on paid losses; and expected loss emergence based on reported losses. The two methods utilized by Regnier to project loss expenses are: paid expenses-to-paid loss and paid expense-to-ultimate loss.

**Pension and Post-retirement Benefit Obligations**

The process of estimating our pension and post-retirement benefit obligations and related benefit expense is inherently uncertain, and the actual cost of benefits may vary materially from the estimates recorded. These liabilities are particularly volatile due to their long-term nature and are based on several assumptions. The main assumptions used in the valuation of our benefit obligations are: estimated mortality of the employees and retirees eligible for benefits; estimated expected long-term rates of return on investments; estimated compensation increases; estimated employee turnover; estimated medical expense trend rate; and estimated rate used to discount the ultimate estimated liability to a present value. We engage a consulting actuary from Principal Financial Group, an independent firm, to assist in evaluating and establishing assumptions used in the valuation of our benefit obligations.

A change in any one or more of these assumptions is likely to result in an ultimate liability different from the original actuarial estimate. Such changes in estimates may be material. For example, a 100 basis point decrease in our estimated discount rate would increase the pension and post-retirement benefit obligation at December 31, 2018,

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by \$34.5 million and \$5.3 million, respectively, while a 100 basis point increase in the rate would decrease the benefit obligation at December 31, 2018, by \$27.3 million and \$4.2 million, respectively.

In addition, for the post-retirement benefit plan, a 100 basis point decrease in the medical trend rate would decrease the post-retirement benefit obligation at December 31, 2018, by \$4.1 million, while a 100 basis point increase in the medical trend rate would increase the benefit obligation at December 31, 2018, by \$5.1 million.

A 100 basis point decrease in our estimated long-term rate of return on pension plan assets would increase the benefit expense for the year ended December 31, 2018, by \$1.6 million, while a 100 basis point increase in the rate would decrease benefit expense by \$1.6 million, for the same period.

For the post-retirement benefit plan, a 100 basis point increase in our estimated medical trend rate would increase the benefit expense for the year ended December 31, 2018, by \$0.7 million, while a 100 basis point decrease in the rate would decrease benefit expense by \$0.5 million, for the same period.

**Recently Issued Accounting Standards**

Information specific to accounting standards that we adopted in 2018 or pending accounting standards that we expect to adopt in the future is incorporated by reference from Note 1 "Summary of Significant Accounting Policies" contained in Part II, Item 8, "Financial Statements and Supplementary Data."

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Information required by this Item 7A is incorporated by reference from Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the headings "Investments" and "Market Risk."

Table of Contents**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**
**United Fire Group, Inc.**  
**Consolidated Balance Sheets**

	<b>December 31,</b>	
	<b>2018</b>	<b>2017</b>
<i>(In Thousands, Except Share Data)</i>		
<b>Assets</b>		
Investments		
Fixed maturities		
Held-to-maturity, at amortized cost (fair value \$0 in 2018 and \$150 in 2017)	\$—	\$ 150
Available-for-sale, at fair value (amortized cost \$1,761,289 in 2018 and \$1,516,610 in 2017)	<b>1,749,488</b>	1,535,070
Trading securities, at fair value (amortized cost \$11,277 in 2018 and \$14,582 in 2017)	<b>13,240</b>	16,842
Equity securities, at fair value (cost \$64,819 in 2018 and \$63,275 in 2017)	<b>248,361</b>	287,344
Mortgage loans	<b>25,782</b>	—
Other long-term investments	<b>37,077</b>	49,352
Short-term investments	<b>175</b>	175
	<b>2,074,123</b>	1,888,933
Cash and cash equivalents	<b>64,454</b>	95,562
Accrued investment income	<b>15,774</b>	13,841
Premiums receivable (net of allowance for doubtful accounts of \$785 in 2018 and \$1,255 in 2017)	<b>346,825</b>	328,513
Deferred policy acquisition costs	<b>92,796</b>	88,102
Property and equipment (primarily land and buildings, at cost, less accumulated depreciation of \$39,894 in 2018 and \$51,603 in 2017)	<b>97,194</b>	68,992
Reinsurance receivables and recoverables	<b>61,337</b>	63,194
Prepaid reinsurance premiums	<b>7,063</b>	3,749
Deferred tax asset	<b>912</b>	—
Income taxes receivable	<b>15,035</b>	6,031
Goodwill and net intangible assets	<b>23,252</b>	23,971
Other assets	<b>17,933</b>	16,409
Assets held for sale	—	1,586,134
<b>Total assets</b>	<b>\$2,816,698</b>	\$4,183,431
<b>Liabilities and stockholders' equity</b>		
<b>Liabilities</b>		
Losses and loss settlement expenses	<b>\$1,312,483</b>	\$1,224,183
Unearned premiums	<b>492,918</b>	465,391
Accrued expenses and other liabilities	<b>122,922</b>	167,396
Deferred income taxes	—	5,953
Liabilities held for sale	—	1,347,135
<b>Total liabilities</b>	<b>\$1,928,323</b>	\$3,210,058
<b>Stockholders' equity</b>		
Common stock, \$0.001 par value; authorized 75,000,000 shares; 25,097,408 and 24,916,806 shares issued and outstanding in 2018 and 2017, respectively	<b>\$25</b>	\$25
Additional paid-in capital	<b>203,350</b>	196,334
Retained earnings	<b>715,472</b>	608,700
Accumulated other comprehensive income (loss), net of tax	<b>(30,472)</b>	168,314
<b>Total stockholders' equity</b>	<b>\$888,375</b>	\$973,373
<b>Total liabilities and stockholders' equity</b>	<b>\$2,816,698</b>	\$4,183,431

The Notes to Consolidated Financial Statements are an integral part of these statements.



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## United Fire Group, Inc.

### Consolidated Statements of Income and Comprehensive Income

	<b>For the Years Ended December 31,</b>		
	<b>2018</b>	2017	2016
<i>(In Thousands, Except Share Data)</i>			
<b>Revenues</b>			
Net premiums earned	<b>\$1,037,451</b>	\$997,492	\$936,131
Investment income, net of investment expenses	<b>52,894</b>	51,190	55,284
Net realized investment gains (losses) (includes reclassifications for net unrealized gains on available-for-sale securities of (\$784) in 2018; \$6,390 in 2017; and \$4,520 in 2016 previously included in accumulated other comprehensive income)	<b>(20,179 )</b>	4,055	4,947
<b>Total revenues</b>	<b>\$1,070,166</b>	\$1,052,737	\$996,362
<b>Benefits, losses and expenses</b>			
Losses and loss settlement expenses	<b>\$731,611</b>	\$725,713	\$652,433
Amortization of deferred policy acquisition costs	<b>206,232</b>	207,746	202,892
Other underwriting expenses (includes reclassifications for employee benefit costs of \$6,642 in 2018; \$5,408 in 2017; and \$5,486 in 2016 previously included in accumulated other comprehensive income)	<b>141,473</b>	103,628	83,540
<b>Total benefits, losses and expenses</b>	<b>\$1,079,316</b>	\$1,037,087	\$938,865
Income (loss) from continuing operations before income taxes	<b>\$ (9,150 )</b>	\$15,650	\$57,497
Federal income tax expense (benefit) (includes reclassifications of \$1,559 in 2018; \$(344) in 2017; and \$338 in 2016 previously included in accumulated other comprehensive income)	<b>(11,405 )</b>	(29,220 )	8,379
<b>Net income from continuing operations</b>	<b>\$2,255</b>	\$44,870	\$49,118
<b>Income (loss) from discontinued operations, net of taxes</b>	<b>(1,912 )</b>	6,153	786
<b>Gain on sale of discontinued operations, net of taxes</b>	<b>27,307</b>	—	—
<b>Net income</b>	<b>\$27,650</b>	\$51,023	\$49,904
<b>Other comprehensive income (loss)</b>			
Change in net unrealized appreciation on investments	<b>\$(50,985 )</b>	\$72,251	\$13,017
Change in liability for underfunded employee benefit plans	<b>25,513</b>	(26,122 )	30,045
Other comprehensive income (loss), before tax and reclassification adjustments	<b>(25,472 )</b>	46,129	43,062
Income tax effect	<b>5,349</b>	(17,540 )	(15,072 )
Other comprehensive income (loss), after tax, before reclassification adjustments	<b>(20,123 )</b>	28,589	27,990
Reclassification adjustment for net realized (gains) losses included in income	<b>784</b>	(6,390 )	(4,520 )
Reclassification adjustment for employee benefit costs included in expense	<b>6,642</b>	5,408	5,486
Total reclassification adjustments, before tax	<b>7,426</b>	(982 )	966
Income tax effect	<b>(1,559 )</b>	344	(338 )
Total reclassification adjustments, after tax	<b>5,867</b>	(638 )	628
<b>Comprehensive income</b>	<b>\$13,394</b>	\$78,974	\$78,522
<b>Weighted average common shares outstanding</b>	<b>25,006,211</b>	25,103,720	25,335,706
<b>Earnings per common share from continuing operations:</b>			
<b>Basic</b>	<b>\$0.09</b>	\$1.79	\$1.94
<b>Diluted</b>	<b>0.09</b>	1.75	1.90
<b>Earnings per common share:</b>			
<b>Basic</b>	<b>\$1.11</b>	\$2.03	\$1.97
<b>Diluted</b>	<b>1.08</b>	1.99	1.93



The Notes to Consolidated Financial Statements are an integral part of these statements.

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United Fire Group, Inc.  
Consolidated Statement of Stockholders' Equity

	For the Years Ended		
	December 31,		
<i>(In Thousands, Except Share Data)</i>	<b>2018</b>	2017	2016
<b>Common stock</b>			
Balance, beginning of year	\$25	\$25	\$25
Shares repurchased (120,372 in 2018; 701,899 in 2017; and 90,415 in 2016)	—	—	—
Shares issued for stock-based awards (300,974 in 2018; 198,694 in 2017; and 376,142 in 2016)	—	—	—
Balance, end of year	\$25	\$25	\$25
<b>Additional paid-in capital</b>			
Balance, beginning of year	\$196,334	\$216,482	\$207,426
Compensation expense and related tax benefit for stock-based award grants	5,249	4,808	2,880
Shares repurchased	(5,404)	(29,784)	(3,746)
Shares issued for stock-based awards	7,171	4,828	9,922
Balance, end of year	\$203,350	\$196,334	\$216,482
<b>Retained earnings</b>			
Balance, beginning of year	\$608,700	\$616,322	\$591,009
Cumulative effect of change in accounting principle	191,244	—	—
Accumulated effect of change in enacted tax rate	—	(31,308)	—
Net unrealized investment depreciation of discontinued operations, sold	(6,714)	—	—
Net income	27,650	51,023	49,904
Dividends on common stock (\$4.21 per share in 2018; \$1.09 per share in 2017; \$0.97 per share in 2016)	(105,408)	(27,337)	(24,591)
Balance, end of year	\$715,472	\$608,700	\$616,322
<b>Accumulated other comprehensive income, net of tax</b>			
Balance, beginning of year	\$168,314	\$109,055	\$80,437
Cumulative effect of change in accounting principle	(191,244)	—	—
Accumulated effect of change in tax enacted tax rate	—	31,308	—
Change in net unrealized investment appreciation <sup>(1)</sup>	(32,944)	44,315	5,523
Change in liability for underfunded employee benefit plans <sup>(2)</sup>	25,402	(16,364)	23,095
Balance, end of year	\$(30,472)	\$168,314	\$109,055
<b>Summary of changes</b>			
Balance, beginning of year	\$973,373	\$941,884	\$878,897
Net income	27,650	51,023	49,904
All other changes in stockholders' equity accounts	(112,648)	(19,534)	13,083
Balance, end of year	\$888,375	\$973,373	\$941,884

(1)The change in net unrealized appreciation is net of reclassification adjustments and income taxes.

(2)The change in liability for underfunded employee benefit plans is net of income taxes.

The Notes to Consolidated Financial Statements are an integral part of these statements.



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## United Fire Group, Inc.

### Consolidated Statements of Cash Flows

	<b>For the Years Ended December 31,</b>		
	<b>2018</b>	2017	2016
<i>(In Thousands)</i>			
<b>Cash Flows From Operating Activities</b>			
Net income	<b>\$ 27,650</b>	\$ 51,023	\$ 49,904
Less net income (loss) from discontinued operations, net of taxes	<b>(1,912)</b>	) 6,153	786
Adjustments to reconcile net income to net cash provided by operating activities			
Net accretion of bond premium	<b>8,788</b>	8,872	7,049
Depreciation and amortization	<b>5,174</b>	4,574	6,035
Stock-based compensation expense	<b>5,249</b>	4,808	3,696
Net realized investment (gains) losses	<b>20,179</b>	(4,055)	) (4,947)
Net cash flows from trading investments	<b>22,514</b>	(1,909)	) (2,390)
Deferred income tax benefit	<b>(16,220)</b>	) (5,921)	) 3,331
Changes in:			
Accrued investment income	<b>(1,933)</b>	) (224)	) (874)
Premiums receivable	<b>(18,312)</b>	) (22,311)	) (29,685)
Deferred policy acquisition costs	<b>(4,694)</b>	) 5,260	(2,815)
Reinsurance receivables	<b>1,857</b>	(487)	) 4,206
Prepaid reinsurance premiums	<b>(3,314)</b>	) 33	8
Income taxes receivable	<b>(9,004)</b>	) 8,254	(14,285)
Other assets	<b>(1,524)</b>	) (2,465)	) 758
Losses, claims and loss settlement expenses	<b>88,300</b>	100,287	120,001
Unearned premiums	<b>27,527</b>	21,589	28,830
Accrued expenses and other liabilities	<b>(12,319)</b>	) (423)	) (7,605)
Income taxes payable	<b>—</b>	—	(5,365)
Deferred income taxes	<b>(10,746)</b>	) (25,883)	) 1,495
Other, net	<b>9,847</b>	3,378	(9,943)
Cash from operating activities - continuing operations	<b>111,369</b>	93,377	97,500
Cash from operating activities - discontinued operations	<b>4,024</b>	31,847	67,766
Cash from operating activities - gain on sale of discontinued operations	<b>(34,851)</b>	) —	—
Total adjustments	<b>\$ 80,542</b>	\$ 125,224	\$ 165,266
Net cash provided by operating activities	<b>\$ 110,104</b>	\$ 170,094	\$ 214,384
<b>Cash Flows From Investing Activities</b>			
Proceeds from sale of available-for-sale investments	<b>\$ 132,250</b>	\$ 7,404	\$ 1,968
Proceeds from call and maturity of held-to-maturity investments	<b>—</b>	150	493
Proceeds from call and maturity of available-for-sale investments	<b>122,250</b>	191,521	323,653
Proceeds from short-term and other investments	<b>9,303</b>	6,032	1,947
Proceeds from sale of discontinued operations	<b>276,055</b>	—	—
Purchase of held-to-maturity investments	<b>—</b>	(150)	) (42)
Purchase of available-for-sale investments	<b>(507,380)</b>	) (260,957)	) (443,953)
Purchase of short-term and other investments	<b>(32,972)</b>	) (6,428)	) (4,155)
Net purchases and sales of property and equipment	<b>(33,053)</b>	) (17,158)	) (7,600)
Cash from investing activities - continuing operations	<b>(33,547)</b>	) (79,586)	) (127,689)
Cash from investing activities - discontinued operations	<b>14,343</b>	17,601	15,286
Net cash used in investing activities	<b>\$ (19,204)</b>	) \$(61,985)	) \$(112,403)
<b>Cash Flows From Financing Activities</b>			
Payment of cash dividends	<b>\$ (105,408)</b>	) \$(27,337)	) \$(24,591)

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Repurchase of common stock	(5,404 )	(29,784 )	(3,746 )
Issuance of common stock	7,171	4,828	9,922
Tax impact from issuance of common stock	—	—	(816 )
Cash from financing activities - continued operations	(103,641 )	(52,293 )	(19,231 )
Cash from financing activities - discontinued operations	(11,547 )	(55,256 )	(78,346 )
Net cash used in financing activities	<b>\$(115,188 )</b>	<b>\$(107,549 )</b>	<b>\$(97,577 )</b>
<b>Net Change in Cash and Cash Equivalents</b>	<b>\$(24,288 )</b>	<b>\$560</b>	<b>\$4,404</b>
<b>Less: decrease (increase) in cash and cash equivalents - discontinued operations</b>	<b>(6,820 )</b>	<b>5,808</b>	<b>(4,706 )</b>
<b>Net increase (decrease) in cash and cash equivalents - continuing operations</b>	<b>(31,108 )</b>	<b>6,368</b>	<b>(302 )</b>
<b>Cash and Cash Equivalents at Beginning of Year - Continuing Operations</b>	<b>95,562</b>	<b>89,194</b>	<b>89,496</b>
<b>Cash and Cash Equivalents at End of Year - Continuing Operations</b>	<b>\$64,454</b>	<b>\$95,562</b>	<b>\$89,194</b>

The Notes to Consolidated Financial Statements are an integral part of these statements.

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**UNITED FIRE GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
*(Amounts in thousands, unless otherwise noted)*

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Business**

United Fire Group, Inc. ("UFG", "United Fire", the "Registrant", the "Company", "we", "us", or "our") and its consolidated subsidiaries and affiliates are engaged in the business of writing property and casualty insurance through a network of independent agencies. Our insurance company subsidiaries are licensed as a property and casualty insurer in 46 states, plus the District of Columbia.

**Discontinued Operations**

We have historically reported our operations in two business segments: property and casualty insurance and life insurance. On September 18, 2017, the Company signed a definitive agreement to sell its subsidiary, United Life Insurance Company ("United Life"), to Kuvare US Holdings, Inc. ("Kuvare") and on March 30, 2018, the sale closed. As a result, our life insurance business, previously a separate segment, was considered held for sale and reported as discontinued operations in the Consolidated Balance Sheets, Consolidated Statements of Income and Comprehensive Income and Consolidated Statements of Cash Flows (collectively, the "Consolidated Financial Statements"). Subsequent to the announcement of this sale, our continuing operations are reported as one business segment. All current and prior periods reflected in this Form 10-K have been presented as continuing and discontinued operations, unless otherwise noted. For more information, refer to Note 17 "Discontinued Operations."

**Principles of Consolidation**

The accompanying Consolidated Financial Statements include United Fire and its wholly owned subsidiaries: United Fire & Casualty Company, United Real Estate Holdings Company, LLC, Addison Insurance Company, Lafayette Insurance Company, United Fire & Indemnity Company, United Fire Lloyds, UFG Specialty Insurance Company, Financial Pacific Insurance Company, Franklin Insurance Company, Mercer Insurance Company, and Mercer Insurance Company of New Jersey, Inc.

United Fire Lloyds, an affiliate of United Fire & Indemnity Company, is organized as a Texas Lloyds plan, which is an aggregation of underwriters who, under a common name, engage in the business of insurance through a corporate attorney-in-fact. United Fire Lloyds is financially and operationally controlled by United Fire & Indemnity Company, its corporate attorney-in-fact, pursuant to three types of agreements: trust agreements between United Fire & Indemnity Company and certain individuals who agree to serve as trustees; articles of agreement among the trustees who agree to act as underwriters to establish how the Lloyds plan will be operated; and powers of attorney from each of the underwriters appointing a corporate attorney-in-fact, who is authorized to operate the Lloyds plan. Because United Fire & Indemnity Company can name the trustees, the Lloyds plan is perpetual, subject only to United Fire & Indemnity Company's desire to terminate it.

United Fire & Indemnity Company provides all of the statutory capital necessary for the formation of the Lloyds plan by contributing capital to each of the trustees. The trust agreements require the trustees to become underwriters of the Lloyds plan, to contribute the capital to the Lloyds plan, to sign the articles of agreement and to appoint the attorney-in-fact. The trust agreements also require the trustees to pay to United Fire & Indemnity Company all of the profits and benefits received by the trustees as underwriters of the Lloyds plan, which means that United Fire & Indemnity Company has the right to receive 100 percent of the gains and profits from the Lloyds plan. The trustees serve at the pleasure of United Fire & Indemnity Company, which may remove a trustee and replace that trustee at any time. Termination of a trustee must be accompanied by the resignation of the trustee as an underwriter, so that the trustee can obtain the capital contribution from the Lloyds plan to reimburse United Fire & Indemnity Company. By retaining the ability to terminate trustees, United Fire & Indemnity Company possesses the ability to name and remove the underwriters.





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United Real Estate Holdings, LLC, formed in 2013, is a wholly owned subsidiary of United Fire & Casualty Company and is organized as an Iowa limited liability corporation, an unincorporated association formed for the purpose of holding United Fire & Casualty Company's ownership in commercial real estate.

### **Basis of Presentation**

The accompanying Consolidated Financial Statements have been prepared on the basis of U.S. generally accepted accounting principles ("GAAP"), which differ in some respects from those followed in preparing our statutory reports to insurance regulatory authorities. Our stand-alone subsidiary financial statements submitted to insurance regulatory authorities are presented on the basis of accounting practices prescribed or permitted by the insurance departments of the states in which we are domiciled ("statutory accounting principles").

### **Use of Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The financial statement categories that are most dependent on management estimates and assumptions include: investments; deferred policy acquisition costs; reinsurance receivables and recoverables; future policy benefits and losses, claims and loss settlement expenses; and pension and post-retirement benefit obligations.

### **Continuing Operations - Property and Casualty Insurance Business**

Premiums written are deferred and recorded as earned premium on a daily pro rata basis over the terms of the respective policies. Unearned premium reserves are established for the portion of premiums written applicable to the unexpired term of insurance policies in force. Premiums receivable are presented net of an estimated allowance for doubtful accounts, which is based on a periodic evaluation of the aging and collectability of amounts due from agents and policyholders.

To establish loss and loss settlement expense reserves, we make estimates and assumptions about the future development of claims. Actual results could differ materially from those estimates, which are subjective, complex and inherently uncertain. When we establish and adjust reserves, we do so given our knowledge at the time of the circumstances and facts of known claims. To the extent that we have overestimated or underestimated our loss and loss settlement expense reserves, we adjust the reserves in the period in which such adjustment is determined. We record our best estimate of reserves for claim litigation that arises in the ordinary course of business. We consider all of our pending litigation as of December 31, 2018 to be ordinary, routine and incidental to our business.

### **Discontinued Operations - Life Insurance Business**

Our whole life and term insurance (i.e., traditional business) premiums are reported as earned when due and benefits and expenses are associated with premium income in order to result in the recognition of profits over the lives of the related contracts. Premiums receivable are presented net of an estimated allowance for doubtful accounts. Income annuities with life contingencies (single premium immediate annuities and supplementary contracts) have premium recorded and any related expense charge fees recorded as income and expense when the contract is issued. On universal life and deferred annuity policies (i.e., non-traditional business), income and expenses are reported when charged and credited to policyholder account balances in order to result in recognition of profits over the lives of the related contracts. We accomplish this by means of a provision for future policy benefits and the deferral and subsequent amortization of policy acquisition costs.

Liabilities for future policy benefits for traditional products are computed by the net level premium method, using interest assumptions ranging from 3.15 percent to 6.0 percent and withdrawal, mortality and morbidity assumptions appropriate at the time the policies were issued. Liabilities for non-traditional business are stated at policyholder account values before surrender charges. Liabilities for traditional immediate annuities are based primarily upon

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future anticipated cash flows using assumptions for mortality and interest rates. Liabilities for deferred annuities are carried at the account value.

**Reinsurance**

Premiums earned and losses and loss settlement expenses incurred are reported net of reinsurance ceded. Ceded insurance business is accounted for on a basis consistent with the original policies issued and the terms of the reinsurance contracts. Refer to Note 4 "Reinsurance" for a discussion of our reinsurance activities.

**Investments**

Investments in fixed maturities include bonds and redeemable preferred stocks. Our investments in held-to-maturity fixed maturities are recorded at amortized cost. Our investments in available-for-sale fixed maturities and trading securities are recorded at fair value.

In 2018, due to the change in accounting principle adopted on January 1, 2018 described in this section under "Recently Issued Accounting Standards," investments in equity securities, which include common and non-redeemable preferred stocks are recorded at fair value with changes in value recorded as a component of income. Prior to 2018, the change in the fair value of equity securities were held as available-for-sale securities and were reported as a component of accumulated other comprehensive income, net of applicable deferred income taxes, in stockholders' equity.

Changes in unrealized appreciation and depreciation, with respect to available-for-sale fixed maturities are reported as a component of accumulated other comprehensive income, net of applicable deferred income taxes, in stockholders' equity. Changes in unrealized appreciation and depreciation, with respect to trading securities, are reported as a component of income.

Other long-term investments consist primarily of our interests in limited liability partnerships that are recorded on the equity method of accounting. Included in investments at December 31, 2018 and 2017, are securities on deposit with, or available to, various regulatory authorities as required by law, with fair values of \$20,456 and \$1,492,928 respectively.

We review all of our investment holdings for appropriate valuation on an ongoing basis. Refer to Note 2 "Summary of Investments" for a discussion of our accounting policy for impairment recognition.

**Cash and Cash Equivalents**

For purposes of reporting cash flows, cash and cash equivalents include cash, money market accounts, and non-negotiable certificates of deposit with original maturities of three months or less.

In 2018, 2017, and 2016, we made cash payments for income taxes of \$29,071, \$7,667 and \$24,034, respectively. In addition, we received federal tax refunds of \$1,503 and \$13,383 in 2018 and 2017, respectively, that resulted from the utilization of our 2011 net operating losses and net capital losses in the carryforward period. In 2016, we did not receive any federal tax refunds. We made no interest payments in 2018, 2017 and 2016. These payments exclude interest credited to policyholders' accounts.

**Deferred Policy Acquisition Costs ("DAC")**

Certain costs associated with underwriting new business (primarily commissions, premium taxes and variable underwriting and policy issue expenses associated with successful acquisition efforts) are deferred. The following table is a summary of the components of DAC that are reported in the accompanying Consolidated Financial Statements.

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Continuing Operations - Property and Casualty Insurance	<b>2018</b>	2017	2016
Recorded asset at beginning of year	<b>\$88,102</b>	\$93,362	\$90,547
Underwriting costs deferred	<b>210,926</b>	202,486	205,707
Amortization of deferred policy acquisition costs	<b>(206,232 )</b>	(207,746 )	(202,892 )
Recorded asset at end of year	<b>\$92,796</b>	\$88,102	\$93,362
Discontinued Operations - Life Insurance			
Recorded asset at beginning of year	<b>\$71,151</b>	\$70,750	\$77,717
Underwriting costs deferred	<b>1,376</b>	5,463	5,564
Amortization of deferred policy acquisition costs	<b>(1,895 )</b>	(5,181 )	(8,121 )
	<b>\$70,632</b>	\$71,032	\$75,160
Change in "shadow" deferred policy acquisition costs	<b>7,274</b>	119	(4,410 )
Sale of discontinued operations	<b>(77,906 )</b>	—	—
Recorded asset at end of year	<b>\$—</b>	\$71,151	\$70,750
Total			
Recorded asset at beginning of year	<b>\$159,253</b>	\$164,112	\$168,264
Underwriting costs deferred	<b>212,302</b>	207,949	211,271
Amortization of deferred policy acquisition costs	<b>(208,127 )</b>	(212,927 )	(211,013 )
	<b>\$163,428</b>	\$159,134	\$168,522
Change in "shadow" deferred policy acquisition costs	<b>7,274</b>	119	(4,410 )
Sale of discontinued operations	<b>(77,906 )</b>	—	—
Recorded asset at end of year	<b>\$92,796</b>	\$159,253	\$164,112

Our continuing operations property and casualty insurance policy acquisition costs deferred are amortized as premium revenue is recognized. The method followed in computing DAC limits the amount of such deferred costs to their estimated realizable value. This takes into account the premium to be earned, losses and loss settlement expenses expected to be incurred and certain other costs expected to be incurred as the premium is earned. This calculation is performed by line of business in a manner consistent with how the policies are currently being marketed and managed.

For the discontinued operations traditional life insurance policies, DAC is amortized to income over the premium-paying period in proportion to the ratio of the expected annual premium revenue to the expected total premium revenue. Expected premium revenue and gross profits are based on the same mortality and withdrawal assumptions used in determining future policy benefits. These assumptions are not revised after policy issuance unless the recorded DAC asset is deemed to be unrecoverable from future expected profits.

For the discontinued operations non-traditional life insurance policies, DAC is amortized over the anticipated terms in proportion to the ratio of the expected annual gross profits to the total expected gross profits. Changes in the amount or timing of expected gross profits result in adjustments to the cumulative amortization of these costs. The effect on amortization of DAC for revisions to estimated gross profits is reported in earnings in the period the estimated gross profits are revised.

The effect on DAC that results from the assumed realization of unrealized gains (losses) on investments allocated to non-traditional life insurance business is recognized with an offset to net unrealized investment appreciation as of the balance sheet date. The impact of unrealized gains (losses) on available-for-sale securities decreased the DAC asset by \$6,294 and \$6,413 at December 31, 2017 and 2016, respectively. There was no impact of unrealized gains and losses on available-for-sale securities on the DAC asset at December 31, 2018 because the non-traditional life insurance business is part of discontinued operations, which was sold on March 30, 2018.



Table of Contents**Property, Equipment and Depreciation**

Property and equipment is presented at cost less accumulated depreciation. The following table is a summary of the components of the property and equipment that are reported in the accompanying Consolidated Financial Statements.

	2018	2017
Real estate:		
Land	\$8,396	\$8,396
Buildings	69,214	48,677
Furniture and fixtures	5,733	4,645
Computer equipment and software	13,851	7,274
Airplane	—	—
Total property and equipment	\$97,194	\$68,992

Expenditures for maintenance and repairs on property and equipment are generally expensed as incurred. We periodically review these assets for impairment whenever events or changes in business circumstances indicate that the carrying value of the underlying asset may not be recoverable. A loss would be recognized if the estimated fair value of the asset were less than its carrying value.

Depreciation is computed primarily by the straight-line method over the following estimated useful lives:

	Useful Life
Computer equipment and software	Three years
Furniture and fixtures	Seven years
Leasehold improvements	Shorter of the lease term or useful life of the asset
Real estate	Seven to thirty-nine years
Airplane	Five years

Depreciation expense totaled \$4,455, \$3,805 and \$5,266 for 2018, 2017 and 2016, respectively.

**Goodwill and Other Intangible Assets**

Goodwill and other intangible assets arise as a result of business combinations and consist of the excess of the fair value of consideration paid over the tangible assets acquired and liabilities assumed. All of our goodwill and the majority of our intangible assets relate to the acquisition of Mercer Insurance Group on March 28, 2011. We evaluate goodwill and other intangible assets for impairment at least on an annual basis or whenever events or changes in circumstances indicate that it is more likely than not that the carrying amount of goodwill and other intangible assets may exceed its implied fair value. Goodwill is evaluated at the reporting unit level. Any impairment is charged to operations in the period that the impairment is identified. In 2016 we performed a quantitative impairment assessment of our goodwill and in 2018 and 2017, we performed a qualitative impairment assessment of our goodwill. As a result of these assessments, we did not recognize an impairment charge on our goodwill in 2018, 2017 or 2016.

Our other intangible assets, which consist primarily of agency relationships, trade names, state insurance licenses, and software, are being amortized by the straight-line method over periods ranging from 2 years to 15 years, with the exception of state insurance licenses, which are indefinite-lived and not amortized. In 2016 we performed a quantitative impairment assessment of our indefinite-lived intangible assets and, in 2018 and 2017, we performed a qualitative impairment assessment of our indefinite lived intangible assets. As a result of these assessments, we did not recognize an impairment charge on our intangible assets in 2018, 2017 and 2016. Amortization expense totaled \$719 in 2018, 2017 and 2016, respectively.

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### **Income Taxes**

The Tax Cuts and Jobs Act of 2017 (the "Tax Act") was enacted on December 22, 2017. The Tax Act significantly revised the U.S. corporate income tax laws including lowering the U.S. federal corporate tax rate from 35 percent to 21 percent, effective January 1, 2018.

In December 2017, the SEC staff issued Staff Accounting Bulletin No. 118, which addresses how a company recognizes provisional amounts when a company does not have the necessary information available, prepared or analyzed in reasonable detail to complete its accounting for the effect of the changes in the Tax Act. The measurement period ends when a company has obtained, prepared and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. As of December 31, 2018 we have completed accounting for the tax effects of enactment of the Tax Act and no adjustments were made during the measurement period.

Deferred tax assets and liabilities are established based on differences between the financial statement bases of assets and liabilities and the tax bases of those same assets and liabilities, using the currently enacted statutory tax rates. Deferred income tax expense is measured by the year-to-year change in the net deferred tax asset or liability, except for certain changes in deferred tax amounts that affect stockholders' equity and do not impact federal income tax expense.

The Company performs a quarterly review of its tax positions and makes a determination whether it is more likely than not that the tax position will be sustained upon examination. If, based on this review, it appears not more likely than not that the position will be sustained, the Company will calculate any unrecognized tax benefits and calculate any interest and penalties. At December 31, 2018, 2017, and 2016 the Company did not recognize any liability for unrecognized tax benefits. In addition, we have not accrued for interest and penalties related to unrecognized tax benefits. However, if interest and penalties would need to be accrued related to unrecognized tax benefits, such amounts would be recognized as a component of federal income tax expense.

We file a consolidated federal income tax return. We also file income tax returns in various state jurisdictions. We are no longer subject to federal or state income tax examination for years before 2015.

### **Stock-Based Compensation**

We currently have two equity compensation plans. One plan allows us to grant restricted and unrestricted stock, stock appreciation rights, incentive stock options, and non-qualified stock options to employees. The other plan allows us to grant restricted and non-qualified stock options to non-employee directors.

We utilize the Black-Scholes option pricing method to establish the fair value of non-qualified stock options granted under our equity compensation plans. Our determination of the fair value of stock options on the date of grant using this option-pricing model is affected by our stock price, as well as assumptions regarding a number of complex and subjective variables, which include the expected volatility in our stock price, the expected term of the award, the expected dividends to be paid over the term of the award and the expected risk-free interest rate. Any changes in these assumptions may materially affect the estimated fair value of the award. For our restricted and unrestricted stock awards, we utilize the fair value of our common stock on the date of grant to establish the fair value of the award. Refer to Note 9 "Stock-Based Compensation" for further discussion.

### **Comprehensive Income**

Comprehensive income includes all changes in stockholders' equity during a period except those resulting from investments by and dividends to stockholders.

### **Subsequent Events**

In the preparation of the accompanying financial statements, the Company has evaluated all material subsequent events or transactions that occurred after the balance sheet date through the date on which the financial statements were issued for potential recognition or disclosure in the Company's financial statements.



Table of Contents**Recently Issued Accounting Standards*****Accounting Standards Adopted in 2018******Revenue Recognition***

In May 2014, the FASB issued comprehensive new guidance on revenue recognition which supersedes nearly all existing revenue recognition guidance under GAAP. The new guidance requires a company to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The standard creates a five-step model that requires companies to exercise judgment when considering the terms of the contract(s) and all relevant facts and circumstances. Insurance contracts are not within the scope of this new guidance. The new guidance is effective for annual and interim periods beginning after December 15, 2017. The Company adopted the guidance as of January 1, 2018. The adoption of the new guidance had no impact on the Company's reporting and disclosure of net premiums earned from insurance contracts, net investment income or net realized gains and losses, as these revenue streams are not within the scope of this new guidance. The remaining revenue streams are immaterial and not impacted by the new standard.

***Financial Instruments***

In January 2016, the FASB issued guidance updating certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The amendments in this update supersede the guidance to classify equity securities with readily determinable fair values into different categories (for example, trading or available-for-sale) and require equity securities to be measured at fair value with changes in the fair value recognized through net income. The new guidance also simplifies the impairment process for equity investments without readily determinable fair values. The new guidance is effective for annual periods beginning after December 15, 2017 and interim periods within those years. The Company adopted the new guidance as of January 1, 2018. The adoption of the new guidance resulted in a reclassification from accumulated other comprehensive income to retained earnings of \$191,244 after tax, which is equal to the amount of net unrealized gains and losses on available-for-sale equity securities on January 1, 2018. Also, in the period ended December 31, 2018, the Company recognized an after-tax net realized investment loss from continuing operations of \$17,375 in net income from the change in value of equity securities in accordance with the adoption of this new accounting guidance.

***Statement of Cash Flows - Classification of Certain Cash Receipts and Payments***

In August 2016, the FASB issued an update that clarifies the classification of certain cash receipts and payments in the Statement of Cash Flows. The update addresses eight existing cash flow issues by clarifying the correct classification to establish uniformity in practice. The updated guidance is effective for annual periods beginning after December 15, 2017 and interim periods within those years. The Company adopted the new guidance as of January 1, 2018. The adoption had no impact on the Company's financial position and results of operations.

***Defined Benefit Retirement Plan Cost***

In March 2017, the FASB issued guidance on the presentation of net periodic benefit costs of defined benefit retirement benefit plans in the Statements of Income. The new guidance requires the service cost component of net periodic benefit cost of defined benefit plans to be presented in the same line in the Statements of Income as other employee compensation expenses. Also, under the new guidance, the service cost component of the net periodic benefit costs will be the only portion of costs subject to be capitalized in assets. The new guidance is effective for annual periods beginning after December 15, 2017 and interim periods within those years. The Company adopted the new guidance as of January 1, 2018. The adoption of the new guidance resulted in a change in the capitalization of deferred acquisition costs to only include the pension and post retirement service costs in place of the total net periodic benefit costs. The adoption had an immaterial impact on the Company's financial position and results of operations. Additionally, the adoption did not impact the Company's presentation in the Statements of Income as all net periodic benefit costs and employee compensation expenses are included within the same category in the Statements of Income.





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*Share-Based Payments*

In May 2017, the FASB issued new guidance which clarifies and addresses the diversity in practice when there is a change in the terms of a share-based payment award. The updated guidance clarifies when to use modification accounting when there is a change in the terms of a share-based payment and provides three conditions where modification accounting should not be applied. The new guidance is effective for annual and interim periods beginning after December 15, 2017. The Company adopted the new guidance as of January 1, 2018. The adoption had no impact on the Company's financial position and results of operations.

***Pending Adoption of Accounting Standards***

*Intangibles - Other Internal Use Software*

In August 2018, the FASB issued guidance to align the requirements for capitalizing implementation costs incurred in a cloud computing hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The guidance requires the Company to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense. The new guidance is effective for annual and interim periods beginning after December 15, 2019. The Company will adopt the new guidance as of January 1, 2020. Management currently believes that the adoption will not have an impact on the Company's financial position or results of operations.

*Leases*

In February 2016, the FASB issued guidance on the accounting for leases. The new guidance requires lessees to place a right-of-use asset and a lease liability on their balance sheets. The lease liability will be based on the present value of the future lease payments and the right-of-use asset will be based on the liability. Expenses will be recognized on the income statement in a similar manner as previous methods. The new guidance also requires companies to classify all leases as operating leases or financing leases. We believe all of our leases will be classified as operating leases. The new guidance is effective for annual periods beginning after December 15, 2018 and interim periods within those years. The Company will adopt the new guidance under a modified retrospective transition approach using the package of practical expedients and the Company will not adopt the hindsight practical expedient as of January 1, 2019. We expect to use the accounting standard adoption date as our date of initial application.

The Company has an inventory of its operating leases and has calculated the total undiscounted future minimum lease payments, which are disclosed in Note 13 "Lease Commitments" of this report. The Company estimates the present value of future minimum lease payments at December 31, 2018 is \$20.1 million, which represents less than 1.0 percent of the Company's total assets at December 31, 2018. The Company will record this amount as a lease liability on their Balance Sheets on January 1, 2019 and an estimated right-of-use asset of \$19.7 million. The Company used their incremental borrowing rate of their credit facility described in Note 14 "Credit Facility" of this Form 10-K, as the discount rate for calculating the present value of the future minimum lease payments where appropriate. For leases that existed prior to the date of initial application or have terms which are not similar to the terms of the credit facility, the Company has elected to use the remaining lease term as of the date of initial application to measure its incremental borrowing rate. In this case, the incremental borrowing rate will be based on current industry borrowing rates for similar Companies with similar ratings.

The Company has a small inventory of property leases for which the Company is the lessor. For these leases, the Company has made the election not to evaluate whether certain sales taxes are the primary obligation of the lessor as owner of the leased asset. The Company has reviewed and updated its processes and controls under the new guidance. Management currently believes that the adoption will not have a significant impact on the Company's financial position or results of operations.

*Financial Instruments - Callable Debt Securities*

In March 2016, the FASB issued an update to amend the amortization period for certain purchased callable debt securities held at a premium. The update requires the premium to be amortized to the earliest call date. The update



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doesn't change the accounting for securities held at a discount, which will continue to be amortized to maturity. The new guidance is effective for annual periods beginning after December 15, 2018 and interim periods beginning after December 15, 2018. The Company will adopt the new guidance as of January 1, 2019. The adoption will have not have a material impact on the Company's financial position and results of operations.

*Income Taxes - Intra-entity Transfers*

In October 2016, the FASB issued new guidance on the income tax treatment of intra-entity transfers. The new guidance replaces the current guidance which prohibits the recognition of current and deferred income taxes of intra-entity transfers until the asset is sold externally. Under the new guidance, the exemption is eliminated and income taxes will be recognized on transfers of intra-entity assets. The new guidance is effective for annual periods beginning after December 15, 2018 and interim periods beginning after December 15, 2019. The Company will adopt the new guidance as of January 1, 2019. Management currently believes that the adoption will have an immaterial impact on the Company's financial position and results of operations.

*Financial Instruments - Credit Losses*

In June 2016, the FASB issued new guidance on the measurement of credit losses for most financial instruments. The new guidance replaces the current incurred loss model for recognizing credit losses with an expected loss model for instruments measured at amortized cost and requires allowances to be recorded for available-for-sale debt securities rather than reduce the carrying amount. These allowances will be remeasured each reporting period. The new guidance is effective for annual periods beginning after December 15, 2019 and interim periods within those years. The new guidance will impact the Company's portfolio of mortgage loan investments which are carried at amortized cost and the impairment model related to our available-for-sale fixed-maturity portfolio. The Company will adopt the new guidance as of January 1, 2020 and is currently evaluating the impact on the Company's financial position, results of operations and key processes.

*Goodwill*

In January 2017, the FASB issued new guidance which simplifies the test for goodwill impairment. The new guidance eliminates the implied fair value calculation when measuring a goodwill impairment charge. Under the new guidance, impairment charges will be based on the excess of the carrying value over fair value of goodwill. The new guidance is effective for annual and interim periods beginning after December 15, 2019. The Company will adopt the new guidance as of January 1, 2020 and it currently believes the adoption will have no impact on the Company's financial position and results of operations.

*Financial Instruments - Disclosures*

In August 2018, the FASB issued new guidance which modifies the disclosure requirements on fair value measurements of financial instruments. The new guidance removes the requirement for disclosing the amount and reason for transfers between Level 1 and Level 2 investment securities and the valuation processes for Level 3 fair value measurements. The guidance also requires additional disclosures on the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. The new guidance is effective for annual and interim periods beginning after December 15, 2019. The Company will adopt the new guidance as of January 1, 2020. Management currently believes the new guidance will modify existing fair value disclosures, but will not have an impact on the Company's financial position and results of operations.

*Defined Benefit Plans - Disclosures*

In August 2018, the FASB issued new guidance which modifies the disclosure requirements for employers that sponsor defined benefit pension and postretirement plans. The new guidance removes the requirement for disclosing the amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit costs in the next year and the sensitivity of postretirement health plans to one-percentage-point changes in medical trend rates. The new guidance is effective for annual periods beginning after December 15, 2019. The Company will adopt the new guidance as of January 1, 2020. Management currently believes the new guidance will

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modify existing disclosures, but will not have an impact on the Company's financial position and results of operations.

**NOTE 2. SUMMARY OF INVESTMENTS****Fair Value of Investments**

The table that follows is a reconciliation of the amortized cost (cost for equity securities) to fair value of investments in held-to-maturity and available-for-sale fixed maturity and available-for-sale equity securities, presented on a consolidated basis, including both continuing and discontinued operations as of December 31, 2018 and 2017.

December 31, 2018

Type of Investment	Cost or Amortized Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
<b>AVAILABLE-FOR-SALE</b>				
Fixed maturities				
Bonds				
U.S. Treasury	\$27,632	\$ 6	\$ 220	\$27,418
U.S. government agency	215,535	896	1,749	214,682
States, municipalities and political subdivisions				
General obligations:				
Midwest	94,806	1,091	685	95,212
Northeast	37,326	432	103	37,655
South	114,710	754	1,553	113,911
West	107,787	1,229	1,175	107,841
Special revenue:				
Midwest	140,025	1,609	870	140,764
Northeast	62,737	452	1,241	61,948
South	237,848	1,669	3,708	235,809
West	143,829	1,294	2,203	142,920
Foreign bonds	9,698	31	13	9,716
Public utilities	56,808	274	1,023	56,059
Corporate bonds				
Energy	28,909	43	304	28,648
Industrials	53,867	124	906	53,085
Consumer goods and services	54,323	142	819	53,646
Health care	16,721	42	105	16,658
Technology, media and telecommunications	26,819	35	678	26,176
Financial services	81,286	238	2,175	79,349
Mortgage-backed securities	7,642	14	232	7,424
Collateralized mortgage obligations				
Government national mortgage association	78,055	380	1,734	76,701
Federal home loan mortgage corporation	108,403	524	1,304	107,623
Federal national mortgage association	53,267	213	732	52,748
Asset-backed securities	3,256	352	113	3,495
<b>Total Available-For-Sale Fixed Maturities</b>	<b>\$1,761,289</b>	<b>\$ 11,844</b>	<b>\$ 23,645</b>	<b>\$1,749,488</b>

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December 31, 2017

Type of Investment	Cost or Amortized Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
<b>HELD-TO-MATURITY</b>				
Fixed maturities				
Bonds				
Corporate bonds - financial services	\$ 150	\$ —	\$ —	\$ 150
Mortgage-backed securities	34	—	—	34
<b>Total Held-to-Maturity Fixed Maturities</b>	<b>\$ 184</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 184</b>
<b>AVAILABLE-FOR-SALE</b>				
Fixed maturities				
Bonds				
U.S. Treasury	\$ 17,073	\$ 4	\$ 186	\$ 16,891
U.S. government agency	121,574	1,311	717	122,168
States, municipalities and political subdivisions				
General obligations:				
Midwest	107,689	2,446	439	109,696
Northeast	47,477	1,174	10	48,641
South	139,870	2,462	813	141,519
West	111,123	2,351	463	113,011
Special revenue:				
Midwest	155,475	3,620	351	158,744
Northeast	79,028	1,351	619	79,760
South	260,145	5,218	1,851	263,512
West	156,576	2,929	1,198	158,307
Foreign bonds	51,361	1,441	49	52,753
Public utilities	206,028	3,386	270	209,144
Corporate bonds				
Energy	93,191	1,972	110	95,053
Industrials	218,067	3,881	241	221,707
Consumer goods and services	183,253	3,498	494	186,257
Health care	74,125	1,312	29	75,408
Technology, media and telecommunications	146,853	2,376	250	148,979
Financial services	277,824	5,769	442	283,151
Mortgage-backed securities	13,828	101	238	13,691
Collateralized mortgage obligations				
Government national mortgage association	157,836	1,921	2,274	157,483
Federal home loan mortgage corporation	201,320	1,879	4,047	199,152
Federal national mortgage association	104,903	1,703	1,174	105,432
Asset-backed securities	4,282	362	8	4,636
<b>Total Available-For-Sale Fixed Maturities</b>	<b>\$ 2,928,901</b>	<b>\$ 52,467</b>	<b>\$ 16,273</b>	<b>\$ 2,965,095</b>

The following table is a reconciliation of the amortized cost (cost for equity securities) to fair value of investments in held-to-maturity and available-for-sale fixed maturity and equity securities for continuing and discontinued operations by investment type at December 31, 2017.



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December 31, 2017

Type of Investment	Cost or Amortized Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
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**HELD-TO-MATURITY**

Fixed maturities:

Continuing operations	\$ 150	\$ —	\$ —	\$ 150
Discontinued operations	34	—	—	34
<b>Total Held-to-Maturity Fixed Maturities</b>	<b>\$ 184</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 184</b>

**AVAILABLE-FOR-SALE**

Fixed maturities:

Continuing operations	\$ 1,516,610	\$ 27,412	\$ 8,952	\$ 1,535,070
Discontinued operations	1,412,291	25,055	7,321	1,430,025
<b>Total Available-for-Sale Fixed Maturities</b>	<b>\$ 2,928,901</b>	<b>\$ 52,467</b>	<b>\$ 16,273</b>	<b>\$ 2,965,095</b>

**Maturities**

The amortized cost and fair value of held-to-maturity, available-for-sale and trading fixed maturity securities at December 31, 2018, by contractual maturity, are shown in the following table. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Asset-backed securities, mortgage-backed securities and collateralized mortgage obligations may be subject to prepayment risk and are therefore not categorized by contractual maturity.

**Maturities**

December 31, 2018	Available-For-Sale		Trading	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$48,331	\$48,492	\$4,408	\$5,232
Due after one year through five years	225,816	226,069	5,019	5,872
Due after five years through 10 years	544,551	542,662	—	—
Due after 10 years	691,968	684,274	1,850	2,136
Asset-backed securities	3,256	3,495	—	—
Mortgage-backed securities	7,642	7,424	—	—
Collateralized mortgage obligations	239,725	237,072	—	—
	<b>\$1,761,289</b>	<b>\$1,749,488</b>	<b>\$11,277</b>	<b>\$13,240</b>

**Net Realized Investment Gains and Losses**

Net realized gains (losses) on disposition of investments are computed using the specific identification method and are included in the computation of net income. A summary of net realized investment gains (losses) for 2018, 2017 and 2016, is as follows:



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	2018	2017	2016
Net realized investment gains (losses) from continuing operations			
Fixed maturities:			
Available-for-sale	<b>\$(254)</b>	\$829	\$1,004
Trading securities			
Change in fair value	<b>(296)</b>	924	189
Sales	<b>1,226</b>	244	931
Equity securities	<b>(20,292)</b>	1,942	2,654
Mortgage loans	<b>(46)</b>	—	—
Cash equivalents	—	—	169
Real estate	<b>(517)</b>	116	—
Total net realized investment gains (losses) from continuing operations	<b>\$(20,179)</b>	\$4,055	\$4,947
Total net realized investment gains (losses) from discontinued operations	<b>(1,057)</b>	4,008	1,156
Total net realized investment gains (losses)	<b>\$(21,236)</b>	\$8,063	\$6,103

The proceeds and gross realized gains (losses) on the sale of available-for-sale fixed maturity securities from continuing operations for 2018, 2017 and 2016, are as follows:

	2018	2017	2016
Proceeds from sales	<b>\$132,250</b>	\$7,404	\$1,968
Gross realized gains	<b>140</b>	1,046	920
Gross realized losses	<b>517</b>	(20)	—

The proceeds and gross realized gains (losses) on the sale of available-for-sale fixed maturity securities from discontinued operations for 2018, 2017 and 2016, are as follows:

	2018	2017	2016
Proceeds from sales	<b>\$</b>	—\$7,315	\$12,354
Gross realized gains	—	1,264	65
Gross realized losses	—	(78)	(639)

There were no sales of held-to-maturity securities in 2018, 2017 and 2016.

Our investment portfolio includes trading securities with embedded derivatives. These securities are primarily convertible securities which are recorded at fair value. Income or loss, including the change in the fair value of these trading securities, is recognized currently in earnings as a component of net realized investment gains and losses. Our portfolio of trading securities had a fair value of \$13,240 and \$16,842 at December 31, 2018 and 2017, respectively.

**Net Investment Income**

Net investment income for the years ended December 31, 2018, 2017 and 2016, is comprised of the following:

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Years Ended December 31,	2018	2017	2016
Investment income from continuing operations:			
Interest on fixed maturities	<b>\$51,356</b>	\$44,784	\$43,147
Dividends on equity securities	<b>7,731</b>	7,108	6,448
Income on other long-term investments			
Investment income	<b>8,383</b>	6,870	1,200
Change in value <sup>(1)</sup>	<b>(10,116 )</b>	(2,812 )	10,178
Interest on mortgage loans	<b>412</b>	—	—
Interest on short-term investments	<b>606</b>	120	47
Interest on cash and cash equivalents	<b>1,875</b>	1,125	352
Other	<b>307</b>	300	422
Total investment income from continuing operations	<b>\$60,554</b>	\$57,495	\$61,794
Less investment expenses	<b>7,660</b>	6,305	6,510
Net investment income from continuing operations	<b>\$52,894</b>	\$51,190	\$55,284
Net investment income from discontinued operations	<b>\$12,663</b>	\$49,720	\$51,538
Net investment income	<b>\$65,557</b>	\$100,910	\$106,822

(1) Represents the change in value of our interests in limited liability partnerships that are recorded on the equity method of accounting.

**Funding Commitment**

At December 31, 2018, pursuant to an agreement with our limited liability partnership investments, we are contractually committed to make capital contributions up to \$22,301 upon request of the partnerships through July 31, 2028.

**Unrealized Appreciation and Depreciation**

A summary of changes in net unrealized investment appreciation for 2018, 2017 and 2016, is as follows for continuing operations and discontinued operations:

	2018	2017	2016
Change in net unrealized investment appreciation			
Available-for-sale fixed maturities	<b>\$(57,475 )</b>	\$25,573	\$(21,271 )
Available-for-sale equity securities	—	40,168	34,179
Deferred policy acquisition costs	<b>7,274</b>	119	(4,410 )
Income tax effect	<b>10,543</b>	(21,545 )	(2,975 )
Cumulative change in accounting principles	<b>(191,244 )</b>	—	—
Accumulated effect of change in enacted tax rate	—	36,658	—
Net unrealized investment depreciation of discontinued operations, sold	<b>6,714</b>	—	—
Total change in net unrealized investment appreciation (depreciation), net of tax	<b>\$(224,188 )</b>	\$80,973	\$5,523

We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires other-than-temporary impairment ("OTTI") charges to be recorded when we determine that it is more likely than not that we will be unable to collect all amounts due according to the contractual terms of the fixed maturity security. Impairment charges on investments are recorded based on the fair value of the investments at the measurement date or based on the value calculated using a discounted cash flow model. Credit-related impairments on fixed maturity securities that we do not plan to sell, and for which we are not more likely than not to be required to sell, are recognized in net income. Any non-credit related impairment is recognized as a component of other comprehensive income. Factors considered in evaluating whether a decline in value is other-than-temporary include: the length of time and the extent to which fair value has been less than cost; the financial condition and near-term prospects of the issuer; our intention to hold the investment; and the likelihood that we will be required to sell the investment.



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The tables on the following pages summarize our fixed maturity and equity securities that were in an unrealized loss position at December 31, 2018 and 2017 for continuing operations and discontinued operations. The securities are presented by the length of time they have been continuously in an unrealized loss position. It is possible that we could recognize OTTI charges in future periods on securities held at December 31, 2018 if future events or information cause us to determine that a decline in fair value is other-than-temporary.

We have evaluated the near-term prospects of the issuers of our fixed maturity securities in relation to the severity and duration of the unrealized loss and determined that these losses did not warrant the recognition of an OTTI charge in 2018, 2017 or 2016. All fixed maturity securities in the investment portfolio continue to pay the expected coupon payments under the contractual terms of the securities. We believe the unrealized depreciation in value of other securities in our fixed maturity portfolio is primarily attributable to changes in market interest rates and not the credit quality of the issuer. We have no intention to sell and it is more likely than not that we will not be required to sell these securities until the fair value recovers to at least equal to our cost basis or the securities mature.

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December 31, 2018	Less than 12 months			12 months or longer			Total	
Type of Investment	Number of Issues	Fair Value	Gross Unrealized Depreciation	Number of Issues	Fair Value	Gross Unrealized Depreciation	Fair Value	Gross Unrealized Depreciation
<b>AVAILABLE-FOR-SALE</b>								
Fixed maturities								
Bonds								
U.S. Treasury	1	\$8,018	\$ 7	5	\$14,645	\$ 213	\$22,663	\$ 220
U.S. government agency	4	17,907	81	17	80,696	1,668	98,603	1,749
States, municipalities and political subdivisions								
General obligations								
Midwest	2	2,939	5	7	23,749	680	26,688	685
Northeast	—	—	—	3	12,110	103	12,110	103
South	1	778	2	22	50,174	1,551	50,952	1,553
West	1	1,203	5	16	48,499	1,170	49,702	1,175
Special revenue								
Midwest	4	3,892	8	19	43,854	862	47,746	870
Northeast	—	—	—	14	37,629	1,241	37,629	1,241
South	4	4,298	30	45	107,016	3,678	111,314	3,708
West	4	11,115	32	28	69,667	2,171	80,782	2,203
Foreign bonds	1	2,984	13	—	—	—	2,984	13
Public utilities	12	25,781	552	8	17,253	471	43,034	1,023
Corporate bonds								
Energy	7	12,556	148	2	4,099	156	16,655	304
Industrials	9	21,970	397	4	11,040	509	33,010	906
Consumer goods and services	14	30,399	527	5	9,554	292	39,953	819
Health care	3	6,203	97	1	345	8	6,548	105
Technology, media and telecommunications	6	12,638	288	5	9,619	390	22,257	678
Financial services	13	30,177	650	13	32,855	1,525	63,032	2,175
Mortgage-backed securities	22	1,539	34	22	4,166	198	5,705	232
Collateralized mortgage obligations								
Government national mortgage association	2	3,797	55	22	44,690	1,679	48,487	1,734
Federal home loan mortgage corporation	3	4,541	20	18	38,189	1,284	42,730	1,304
Federal national mortgage association	4	2,107	3	15	38,986	729	41,093	732
Asset-backed securities	1	2,829	113	—	—	—	2,829	113
<b>Total Available-for-Sale Fixed Maturities</b>	<b>118</b>	<b>\$207,671</b>	<b>\$ 3,067</b>	<b>291</b>	<b>\$698,835</b>	<b>\$ 20,578</b>	<b>\$906,506</b>	<b>\$ 23,645</b>

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December 31, 2017	Less than 12 months			12 months or longer			Total	
Type of Investment	Number of Issues	Fair Value	Gross Unrealized Depreciation	Number of Issues	Fair Value	Gross Unrealized Depreciation	Fair Value	Gross Unrealized Depreciation
<b>AVAILABLE-FOR-SALE</b>								
Fixed maturities								
Bonds								
U.S. Treasury	5	\$ 10,370	\$ 67	2	\$ 5,765	\$ 119	\$ 16,135	\$ 186
U.S. government agency	11	64,842	390	5	19,372	327	84,214	717
States, municipalities and political subdivisions								
General obligations								
Midwest	2	2,177	8	3	19,729	431	21,906	439
Northeast	—	—	—	1	3,644	10	3,644	10
South	3	7,959	32	11	29,545	781	37,504	813
West	2	5,944	18	8	25,755	445	31,699	463
Special revenue								
Midwest	2	3,486	15	7	19,130	336	22,616	351
Northeast	1	4,471	37	11	28,476	582	32,947	619
South	8	7,749	107	27	69,917	1,744	77,666	1,851
West	3	5,424	16	22	56,753	1,182	62,177	1,198
Foreign bonds	1	857	49	—	—	—	857	49
Public utilities	8	19,186	79	5	8,446	191	27,632	270
Corporate bonds								
Energy	1	2,236	13	1	1,606	97	3,842	110
Industrials	10	27,773	146	2	4,275	95	32,048	241
Consumer goods and services	14	32,781	248	3	6,813	246	39,594	494
Health care	4	9,947	29	—	—	—	9,947	29
Technology, media and telecommunications	12	35,319	122	3	10,413	128	45,732	250
Financial services	22	50,144	256	4	11,389	186	61,533	442
Mortgage-backed securities	10	2,458	18	10	6,641	220	9,099	238
Collateralized mortgage obligations								
Government national mortgage association	20	49,764	629	17	46,969	1,645	96,733	2,274
Federal home loan mortgage corporation	11	37,543	577	20	75,679	3,470	113,222	4,047
Federal national mortgage association	11	31,958	342	11	20,123	832	52,081	1,174
Asset-backed securities	1	992	8	—	—	—	992	8
<b>Total Available-for-Sale Fixed Maturities</b>	<b>162</b>	<b>\$ 413,380</b>	<b>\$ 3,206</b>	<b>173</b>	<b>\$ 470,440</b>	<b>\$ 13,067</b>	<b>\$ 883,820</b>	<b>\$ 16,273</b>

The following tables are a reconciliation for continuing and discontinued operations of our total fixed maturity and equity securities that were in an unrealized loss position at December 31, 2017. The securities are presented by the length of time they have been continuously in an unrealized loss position:

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December 31, 2017	Less than 12 months			12 months or longer			Total	
Type of Investment	Number of Issues	Fair Value	Gross Unrealized Depreciation	Number of Issues	Fair Value	Gross Unrealized Depreciation	Fair Value	Gross Unrealized Depreciation
<b>AVAILABLE-FOR-SALE</b>								
Fixed maturities:								
Continuing operations	88	\$232,489	\$ 1,791	112	\$302,815	\$ 7,161	\$535,304	\$ 8,952
Discontinued operations	74	180,891	1,415	61	167,625	5,906	348,516	7,321
<b>Total Available-for-Sale Fixed Maturities</b>	<b>162</b>	<b>\$413,380</b>	<b>\$ 3,206</b>	<b>173</b>	<b>\$470,440</b>	<b>\$ 13,067</b>	<b>\$883,820</b>	<b>\$ 16,273</b>

**NOTE 3. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Current accounting guidance on fair value measurements includes the application of a fair value hierarchy that requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Our financial instruments that are recorded at fair value are categorized into a three-level hierarchy, which is based upon the priority of the inputs to the valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets (i.e., Level 1) and the lowest priority to unobservable inputs (i.e., Level 3). If the inputs used to measure fair value fall within different levels of the hierarchy, the category level is based on the lowest priority level input that is significant to the fair value measurement of the financial instrument. Financial instruments recorded at fair value are categorized in the fair value hierarchy as follows:

*Level 1:* Valuations are based on unadjusted quoted prices in active markets for identical financial instruments that we have the ability to access.

*Level 2:* Valuations are based on quoted prices for similar financial instruments, other than quoted prices included in Level 1, in markets that are not active or on inputs that are observable either directly or indirectly for the full term of the financial instrument.

*Level 3:* Valuations are based on pricing or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement of the financial instrument. Such inputs may reflect management's own assumptions about the assumptions a market participant would use in pricing the financial instrument.

We review our fair value hierarchy categorizations on a quarterly basis at which time the classification of certain financial instruments may change if the input observations have changed. Transfers between levels, if any, are recorded as of the beginning of the reporting period.

To determine the fair value of the majority of our investments, we utilize prices obtained from independent, nationally recognized pricing services. We obtain one price for each security. When the pricing services cannot provide a determination of fair value for a specific security, we obtain non-binding price quotes from broker-dealers with whom we have had several years experience and who have demonstrated knowledge of the subject security. We request and utilize one broker quote per security.

In order to determine the proper classification in the fair value hierarchy for each security where the price is obtained from an independent pricing service, we obtain and evaluate the vendors' pricing procedures and inputs used to price the security, which include unadjusted quoted market prices for identical securities, such as a New York Stock Exchange closing price, and quoted prices for identical securities in markets that are not active. For fixed maturity securities, an evaluation of interest rates and yield curves observable at commonly quoted intervals, volatility, prepayment speeds, credit risks and default rates may also be performed. We have determined that these processes and inputs result in fair values and classifications consistent with the applicable accounting guidance on fair value measurements.





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When possible, we use quoted market prices to determine the fair value of fixed maturities, equity securities, trading securities and short-term investments. When quoted market prices do not exist, we base estimates of fair value on market information obtained from independent pricing services and brokers or on valuation techniques that are both unobservable and significant to the overall fair value measurement of the financial instrument. Such inputs may reflect management's own assumptions about the assumptions a market participant would use in pricing the financial instrument. Our valuation techniques are discussed in more detail throughout this section.

The fair value of our mortgage loans is determined by modeling performed by us based on the stated principal and coupon payments provided for in the loan agreements. These cash flows are then discounted using an appropriate risk-adjusted discount rate to determine the loan's fair value, which is a Level 3 fair value measurement.

The fair value of our policy loans is equivalent to carrying value, which is a reasonable estimate of fair value and is classified as Level 2. We do not make policy loans for amounts in excess of the cash surrender value of the related policy. In all instances, the policy loans are fully collateralized by the related liability for future policy benefits for traditional insurance policies or by the policyholders' account balance for non-traditional policies.

Our other long-term investments consist primarily of our interests in limited liability partnerships that are recorded on the equity method of accounting. The fair value of the partnerships is obtained from the fund managers, which is based on the fair value of the underlying investments held in the partnerships. In management's opinion, these values represent a reasonable estimate of fair value. We have not adjusted the net asset value provided by the fund managers. For cash and cash equivalents and accrued investment income, carrying value is a reasonable estimate of fair value due to the short-term nature of these financial instruments.

The Company formed a rabbi trust in 2014 to fund obligations under the United Fire & Casualty Company Non-qualified Deferred Compensation Plan and United Fire Group Supplemental Executive Retirement and Deferral Plan (collectively the "Executive Retirement Plans"). Within the rabbi trust, corporate-owned life insurance ("COLI") policies are utilized as an investment vehicle and source of funding for the Company's Executive Retirement Plans. The COLI policies invest in mutual funds, which are priced daily by independent sources. As of December 31, 2018, the cash surrender value of the COLI policies was \$4,907, which is equal to the fair value measured using Level 2 inputs, based on the underlying assets of the COLI policies, and is included in other assets in the Consolidated Balance Sheets.

Policy reserves are developed and recorded for deferred annuities, which is an interest-sensitive product, and income annuities. The fair value of the reserve liability for these annuity products is based upon an estimate of the discounted pretax cash flows that are forecast for the underlying business, which is a Level 3 fair value measurement. We base the discount rate on the current U.S. Treasury spot yield curve, which is then risk-adjusted for nonperformance risk and, for interest-sensitive business and market risk factors. The risk-adjusted discount rate is developed using interest rates that are available in the market and representative of the risks applicable to the underlying business.



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A summary of the carrying value and estimated fair value of our financial instruments from continuing operations at December 31, 2018 and 2017 is as follows:

	<b>December 31, 2018</b>		December 31, 2017	
	<b>Fair Value</b>	<b>Carrying Value</b>	Fair Value	Carrying Value
<b>Assets</b>				
Investments				
Fixed maturities:				
Held-to-maturity securities	\$ —	\$ —	\$ 150	\$ 150
Available-for-sale securities	<b>1,749,488</b>	<b>1,749,488</b>	1,535,070	1,535,070
Trading securities	<b>13,240</b>	<b>13,240</b>	16,842	16,842
Equity securities:	<b>248,361</b>	<b>248,361</b>	287,344	287,344
Mortgage loans	<b>26,021</b>	<b>25,782</b>	—	—
Other long-term investments	<b>37,077</b>	<b>37,077</b>	49,352	49,352
Short-term investments	<b>175</b>	<b>175</b>	175	175
Cash and cash equivalents	<b>64,454</b>	<b>64,454</b>	95,562	95,562
Corporate-owned life insurance	<b>4,907</b>	<b>4,907</b>	4,029	4,029

A summary of the carrying value and estimated fair value of our financial instruments from discontinued operations at December 31, 2018 and 2017 is as follows:

	<b>December 31, 2018</b>		December 31, 2017	
	<b>Fair Value</b>	<b>Carrying Value</b>	Fair Value	Carrying Value
<b>Assets</b>				
Investments				
Fixed maturities:				
Held-to-maturity securities	\$ —	\$ —	\$ 34	\$ 34
Available-for-sale securities	—	—	1,430,025	1,430,025
Equity securities:				
Available-for-sale securities	—	—	23,653	23,653
Mortgage loans	—	—	3,594	3,435
Policy loans	—	—	5,815	5,815
Other long-term investments	—	—	16,437	16,437
Cash and cash equivalents	—	—	15,851	15,851
<b>Liabilities</b>				
Policy reserves				
Annuity (accumulations) <sup>(1)</sup>	\$ —	\$ —	\$ 591,702	\$ 611,866
Annuity (benefit payments)	—	—	147,038	93,560



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The following tables present the categorization for our financial instruments measured at fair value on a recurring basis. The tables include financial instruments from both continuing and discontinued operations at December 31, 2018 and 2017:

Description	December 31, 2018	Fair Value Measurements		
		Level 1	Level 2	Level 3
<b>AVAILABLE-FOR-SALE</b>				
Fixed maturities				
Bonds				
U.S. Treasury	\$ 27,418	\$—	\$ 27,418	\$—
U.S. government agency	214,682	—	214,682	—
States, municipalities and political subdivisions				
General obligations				
Midwest	95,212	—	95,212	—
Northeast	37,655	—	37,655	—
South	113,911	—	113,911	—
West	107,841	—	107,841	—
Special revenue				
Midwest	140,764	—	140,764	—
Northeast	61,948	—	61,948	—
South	235,809	—	235,809	—
West	142,920	—	142,920	—
Foreign bonds				
Public utilities	56,059	—	56,059	—
Corporate bonds				
Energy	28,648	—	28,648	—
Industrials	53,085	—	53,085	—
Consumer goods and services	53,646	—	53,646	—
Health care	16,658	—	16,658	—
Technology, media and telecommunications	26,176	—	26,176	—
Financial services	79,349	—	79,099	250
Mortgage-backed securities				
Collateralized mortgage obligations				
Government national mortgage association	76,701	—	76,701	—
Federal home loan mortgage corporation	107,623	—	107,623	—
Federal national mortgage association	52,748	—	52,748	—
Asset-backed securities	3,495	—	2,829	666
<b>Total Available-For-Sale Fixed Maturities</b>	<b>\$ 1,749,488</b>	<b>\$—</b>	<b>\$ 1,748,572</b>	<b>\$ 916</b>
<b>TRADING</b>				
Fixed maturities				
Bonds				
Corporate bonds				
Industrials	\$ 397	\$—	\$ 397	\$—
Consumer goods and services	1,599	—	1,599	—
Health care	3,236	—	3,236	—
Technology, media and telecommunications	3,028	—	3,028	—
Financial services	2,231	—	2,231	—
Redeemable preferred stocks	2,749	2,749	—	—
<b>Total Trading Securities</b>	<b>\$ 13,240</b>	<b>\$ 2,749</b>	<b>\$ 10,491</b>	<b>\$—</b>

**Equity securities**

Public utilities	<b>15,949</b>	<b>15,949</b>	—	—
Energy	<b>10,975</b>	<b>10,975</b>	—	—
Industrials	<b>53,536</b>	<b>53,536</b>	—	—
Consumer goods and services	<b>24,465</b>	<b>24,465</b>	—	—
Health care	<b>22,286</b>	<b>22,286</b>	—	—
Financial Services	<b>101,555</b>	<b>101,555</b>	—	—

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Technology, media and telecommunications	<b>13,944</b>	<b>13,944</b>	—	—
Nonredeemable preferred stocks	<b>5,651</b>	<b>5,056</b>	—	<b>595</b>
<b>Total Equity Securities</b>	<b>\$248,361</b>	<b>\$247,766</b>	<b>\$—</b>	<b>\$595</b>
<b>Short-Term Investments</b>	<b>\$175</b>	<b>\$175</b>	<b>\$—</b>	<b>\$—</b>
<b>Money Market Accounts</b>	<b>\$3,275</b>	<b>\$3,275</b>	<b>\$—</b>	<b>\$—</b>
<b>Corporate-Owned Life Insurance</b>	<b>\$4,907</b>	<b>\$—</b>	<b>\$4,907</b>	<b>\$—</b>
<b>Total Assets Measured at Fair Value</b>	<b>\$2,019,446</b>	<b>\$253,965</b>	<b>\$1,763,970</b>	<b>\$1,511</b>

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Description	December 31, 2017	Fair Value Measurements		
		Level 1	Level 2	Level 3
<b>AVAILABLE-FOR-SALE</b>				
Fixed maturities				
Bonds				
U.S. Treasury	\$ 16,891	\$—	\$ 16,891	\$—
U.S. government agency	122,168	—	122,168	—
States, municipalities and political subdivisions				
General obligations				
Midwest	109,696	—	109,696	—
Northeast	48,641	—	48,641	—
South	141,519	—	141,519	—
West	113,011	—	113,011	—
Special revenue				
Midwest	158,744	—	158,744	—
Northeast	79,760	—	79,760	—
South	263,512	—	263,512	—
West	158,307	—	158,307	—
Foreign bonds	52,753	—	52,753	—
Public utilities	209,144	—	209,144	—
Corporate bonds				
Energy	95,053	—	95,053	—
Industrials	221,707	—	221,707	—
Consumer goods and services	186,257	—	185,589	668
Health care	75,408	—	75,408	—
Technology, media and telecommunications	148,979	—	148,979	—
Financial services	283,151	—	275,474	7,677
Mortgage-backed securities	13,691	—	13,691	—
Collateralized mortgage obligations				
Government national mortgage association	157,483	—	157,483	—
Federal home loan mortgage corporation	199,152	—	199,152	—
Federal national mortgage association	105,432	—	105,432	—
Asset-backed securities	4,636	—	3,989	647
Total Available-For-Sale Fixed Maturities	\$ 2,965,095	\$—	\$ 2,956,103	\$ 8,992
<b>TRADING</b>				
Fixed maturities				
Bonds				
Corporate bonds				
Industrials	\$ 2,220	\$—	\$ 2,220	\$—
Consumer goods and services	1,535	—	1,535	—
Health care	3,741	—	3,741	—
Technology, media and telecommunications	1,221	—	1,221	—
Financial services	5,566	—	5,566	—
Redeemable preferred stocks	2,559	2,559	—	—
Total Trading Securities	\$ 16,842	\$ 2,559	\$ 14,283	\$—
Equity securities				
Public utilities	\$ 23,313	\$ 23,313	\$—	\$—
Energy	14,755	14,755	—	—



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Industrials	67,508	67,506	2	—
Consumer goods and services	27,002	27,002	—	—
Health care	40,428	40,428	—	—
Financial Services	116,645	116,645	—	—

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Technology, media and telecommunications	17,508	17,508	—	—
Nonredeemable preferred stocks	3,838	2,956	—	882
Total Equity Securities	\$310,997	\$310,113	\$2	\$882
Short-Term Investments	\$175	\$175	\$—	\$—
Money Market Accounts	\$16,824	\$16,824	\$—	\$—
Corporate-Owned Life Insurance	\$4,029	\$—	\$4,029	\$—
Total Assets Measured at Fair Value	\$3,313,962	\$329,671	\$2,974,417	\$9,874



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The following tables are a reconciliation for both continuing and discontinued operations of the presentation of the categorization for our financial instruments measured at fair value on a recurring basis at December 31, 2017:

December 31, 2017 Description	Fair Value Measurements			
	Total	Level 1	Level 2	Level 3
<b>AVAILABLE-FOR-SALE</b>				
Continuing operations	\$ 1,535,070	\$—	\$ 1,534,323	\$747
Discontinued operations	1,430,025	—	1,421,780	8,245
<b>Total Available-for-Sale</b>	<b>\$2,965,095</b>	<b>\$—</b>	<b>\$2,956,103</b>	<b>\$8,992</b>
<b>TRADING</b>				
Continuing operations	\$ 16,842	\$2,559	\$ 14,283	\$—
Discontinued operations	—	—	—	—
<b>Total Trading Securities</b>	<b>\$ 16,842</b>	<b>\$2,559</b>	<b>\$ 14,283</b>	<b>\$—</b>
<b>EQUITY SECURITIES:</b>				
Continuing operations	\$287,344	\$286,462	\$—	\$882
Discontinued operations	23,653	23,651	2	—
<b>Equity securities</b>	<b>\$310,997</b>	<b>\$310,113</b>	<b>\$2</b>	<b>\$882</b>
<b>SHORT-TERM INVESTMENTS</b>				
Continuing operations	\$ 175	\$ 175	\$—	\$—
Discontinued operations	—	—	—	—
<b>Short-Term Investments</b>	<b>\$ 175</b>	<b>\$ 175</b>	<b>\$—</b>	<b>\$—</b>
<b>MONEY MARKET ACCOUNTS</b>				
Continuing operations	\$6,147	\$6,147	\$—	\$—
Discontinued operations	10,677	10,677	—	—
<b>Money Market Accounts</b>	<b>\$ 16,824</b>	<b>\$ 16,824</b>	<b>\$—</b>	<b>\$—</b>
<b>CORPORATE-OWNED LIFE INSURANCE</b>				
Continuing operations	\$4,029	\$—	\$4,029	\$—
Discontinued operations	—	—	—	—
<b>Corporate-Owned Life Insurance</b>	<b>\$4,029</b>	<b>\$—</b>	<b>\$4,029</b>	<b>\$—</b>
<b>Total Assets Measured at Fair Value</b>	<b>\$3,313,962</b>	<b>\$329,671</b>	<b>\$2,974,417</b>	<b>\$9,874</b>

The fair value of securities that are categorized as Level 1 is based on quoted market prices that are readily and regularly available.

We use a market-based approach for valuing all of our Level 2 securities and receive them primarily from a third-party valuation service provider. Any of these securities not valued by this service provider are submitted to another third-party valuation service provider for pricing. Both service providers use a market approach to find pricing of similar financial instruments. The market inputs our service providers normally seek to value our securities include the following, listed in approximate order of priority: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications. The method and inputs for these securities classified as Level 2 are the same regardless of industry category, credit quality, duration, geographical concentration or economic characteristics. For our mortgage-backed securities, collateralized mortgage obligations and asset-backed securities, our service providers use additional market inputs to value these securities, including the following: new issue data, periodic payment information, monthly payment information, collateral performance and real estate analysis from third parties. Our service providers prioritize inputs based on market conditions, and not all inputs listed are available for use in the valuation process for each security on any given day.



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At least annually, we review the methodologies and assumptions used by our valuation service providers and verify that they are reasonable and representative of the fair value of the underlying securities held in the investment portfolio. We validate the prices obtained from independent pricing services and brokers prior to their use for reporting purposes by evaluating their reasonableness on a monthly basis. Our validation process includes a review for unusual fluctuations. Unusual fluctuations outside of our expectations are independently corroborated with additional third-party sources that use similar valuation techniques as discussed above. In addition, we also test the all securities in the portfolio and independently corroborate the valuations obtained from our third-party valuation service providers. We also perform deep dive analysis of the pricing method used by our third-party valuation service provider by selecting a random sample of securities by asset class. In our opinion, the pricing obtained at December 31, 2018 and 2017 was reasonable.

For the year ended December 31, 2018, the change in our available-for-sale securities categorized as Level 1 and Level 2 is the result of investment purchases that were made using funds held in our money market accounts, disposals and the change in unrealized gains on both fixed maturities and equity securities. During the twelve month period ended December 31, 2018, there were no securities transferred between Level 1 and Level 2. Securities categorized as Level 3 include holdings in certain private placement fixed maturity and equity securities for which an active market does not currently exist. The fair value of our Level 3 private placement securities is determined by management relying on pricing received from our independent pricing services and brokers consistent with the process to estimate fair value for Level 2 securities. However, securities are categorized as Level 3 if these quotes cannot be corroborated by other market observable data due to the unobservable nature of the brokers' valuation processes. If pricing cannot be obtained from these sources, which occurs on a limited basis, management will perform a discounted cash flow analysis, using an appropriate risk-adjusted discount rate, on the underlying security to estimate fair value. During the twelve month period ended December 31, 2018 and 2017, there were no securities transferred in or out of Level 3.

The following table provides a summary of the changes in fair value of our Level 3 securities, from continuing operations for 2018:

	Corporate bonds	Asset-backed securities	Equities	Total
Balance at January 1, 2018	\$ 100	\$ 647	\$ 882	\$ 1,629
Unrealized gains (losses) <sup>(1)</sup>	—	19	(287 )	(268 )
Purchases	150	—	—	150
Balance at December 31, 2018	\$ 250	\$ 666	\$ 595	\$ 1,511

(1) Unrealized gains (losses) are recorded as a component of comprehensive income.

The following table provides a summary of the changes in fair value of our Level 3 securities, from both continuing and discontinued operations for 2017:

	States, municipalities and political subdivisions	Corporate bonds	Asset-backed securities	Equities	Total
Balance at January 1, 2017	\$ 168	\$ 9,894	\$ 449	\$ 4,587	\$ 15,098
Unrealized gains (losses) <sup>(1)</sup>	(8 )	(129 )	198	287	348
Purchases	—	100	—	145	245
Disposals	(160 )	(1,520 )	—	(4,137 )	(5,817 )
Balance at December 31, 2017	\$ —	\$ 8,345	\$ 647	\$ 882	\$ 9,874

(1) Realized gains (losses) are recorded as a component of earnings, whereas unrealized gains (losses) are recorded as a component of comprehensive income.



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The fixed maturities reported as disposals relate to the receipt of principal on calls or sinking fund bonds, in accordance with the indentures.

**Commercial Mortgage Loans**

The following tables present the carrying value of our commercial mortgage loans and additional information at December 31, 2018 and 2017:

**Commercial Mortgage Loans**

	December 31, 2018	December 31, 2017
<b>Loan-to-value</b>		
Less than 65%	\$ 25,828	—
<b>Total amortized cost</b>	<b>\$ 25,828</b>	<b>\$ —</b>
<b>Valuation allowance (46 )</b>		—
<b>Total mortgage loans</b>	<b>\$ 25,782</b>	<b>\$ —</b>

**Mortgage Loans by Region**

	December 31, 2018		December 31, 2017	
	Carrying Value	Percent of Total	Carrying Value	Percent of Total
East North Central	\$3,244	12.6 %	\$ —	—%
Southern Atlantic	6,652	25.8	—	—
East South Central	4,975	19.3	—	—
New England	6,588	25.4	—	—
Middle Atlantic	4,369	16.9	—	—
<b>Total mortgage loans at amortized cost</b>	<b>\$25,828</b>	<b>100.0 %</b>	<b>\$ —</b>	<b>—%</b>

**Mortgage Loans by Property Type**

	December 31, 2018		December 31, 2017	
	Carrying Value	Percent of Total	Carrying Value	Percent of Total
Commercial				
Multifamily	\$3,244	12.6 %	\$ —	—%
Office	11,627	45.0	—	—
Mixed use/Other	10,957	42.4	—	—
<b>Total mortgage loans at amortized cost</b>	<b>\$25,828</b>	<b>100.0 %</b>	<b>\$ —</b>	<b>—%</b>

**Mortgage Loan Valuation Allowance**

The commercial mortgage loans originate with an initial loan-to-value ratio to provide sufficient collateral to absorb losses should a loan be required to foreclose. Mortgage loans are evaluated on a quarterly basis for impairment on an individual basis through a monitoring process and review of key credit indicators, such as economic trends, delinquency rates, property valuations, occupancy and rental rates and loan-to-value ratios. A loan is considered impaired when the Company believes it will not collect the contractual principal and interest set forth in the contractual terms of the loan. A valuation allowance is established on each loan recognizing a loss for amounts which we believe will not be collected according to the contractual terms of the respective loan agreement. For the year end December 31, 2018 the Company had a valuation allowance of \$46.





Table of Contents**NOTE 4. REINSURANCE****Continuing Operations - Property and Casualty Insurance Business*****Ceded and Assumed Reinsurance***

Reinsurance is a contract by which one insurer, called the reinsurer, agrees to cover, under certain defined circumstances, a portion of the losses incurred by a primary insurer if a claim is made under a policy issued by the primary insurer. Our property and casualty insurance companies follow the industry practice of reinsuring a portion of their exposure by ceding to reinsurers a portion of the premium received and a portion of the risk under the policies written. We purchase reinsurance to reduce the net liability on individual risks to predetermined limits and to protect us against catastrophic losses, such as a hurricane or tornado. We do not engage in any reinsurance transactions classified as finite risk reinsurance.

We account for premiums, written and earned, and losses incurred net of reinsurance ceded. The ceding of insurance does not legally discharge us from primary liability under our policies, and we must pay the loss if the reinsurer fails to meet its obligation. We periodically monitor the financial condition of our reinsurers to confirm that they are financially stable. We believe that all of our reinsurers are in an acceptable financial condition and there were no reinsurance balances at December 31, 2018 for which collection is at risk that would result in a material impact on our Consolidated Financial Statements. The amount of reinsurance recoverable on paid losses totaled \$3,779 and \$2,859 at December 31, 2018 and 2017, respectively.

We also assume both property and casualty insurance from other insurance or reinsurance companies. Most of the business we have assumed is property insurance, with an emphasis on catastrophe coverage.

Premiums and losses and loss settlement expenses related to our ceded and assumed business are as follows:

Years Ended December 31,	<b>2018</b>	2017	2016
<b>Ceded Business</b>			
Ceded premiums written	<b>\$66,800</b>	\$61,273	\$57,988
Ceded premiums earned	<b>63,487</b>	61,305	57,996
Loss and loss settlement expenses ceded	<b>22,317</b>	33,303	13,278
<b>Assumed Business</b>			
Assumed premiums written	<b>\$16,761</b>	\$15,179	\$16,834
Assumed premiums earned	<b>16,957</b>	15,059	17,037
Loss and loss settlement expenses assumed	<b>(3,954 )</b>	24,688	9,814

In 2018, we renewed our participation in all of our assumed programs. Loss and loss settlement expenses decreased in 2018 compared to 2017 as we remain conservative in our reserving approach, and during the year we reviewed our book of business and released excess reserves. During 2018 for ceded business, ceded loss and loss settlement expenses decreased primarily due to commercial auto, commercial property, and catastrophe losses staying in our retention lowering our ceded recoverable amounts.

In 2017, we renewed our participation in all of our assumed programs. Loss and loss settlement expenses ceded increased in 2017 as compared to 2016, primarily due to an increase in severity of commercial auto losses, assumed reinsurance losses and catastrophe losses.

In 2016, we renewed our participation in all of our assumed programs.

Refer to Note 5 "Reserves for Losses and Loss Settlement Expenses" for an analysis of changes in our overall property and casualty insurance reserves.



Table of Contents**Reinsurance Programs and Retentions**

We have several programs that provide reinsurance coverage. This reinsurance coverage limits the risk of loss that we retain by reinsuring direct risks in excess of our retention limits. The following table provides a summary of our primary reinsurance programs. Retention amounts reflect the accumulated retentions and co-participation of all layers within a program. For 2018, there was an all lines annual aggregate excess of loss program with variable retention of 6.78 percent of gross net earned premium with a minimum retention of \$58.5 million and a maximum of \$71.5 million. Our all lines aggregate recovery is also limited to \$30.0 million. For 2017, there was an all lines annual aggregate excess of loss program with a variable retention of 7.02 percent of gross net earned premium with a minimum retention of \$58.5 million and a maximum of \$71.5 million. Our all lines aggregate recovery is also limited to a maximum of \$30.0 million. For 2016, there was an all lines annual aggregate excess of loss program with a variable retention of 7.73 percent of gross net earned premium with a minimum retention of \$52.0 million and a maximum of \$65.0 million. Our all lines aggregate recovery is also limited to a maximum of \$30.0 million.

2018 Reinsurance Programs			
Type of Reinsurance	Stated Retention	Limits	Coverage
Casualty excess of loss	<b>\$2,500</b>	<b>\$60,000</b>	<b>100 % of \$57,500</b>
Property excess of loss	<b>2,500</b>	<b>25,000</b>	<b>100 % of \$22,500</b>
Surety excess of loss	<b>1,500</b>	<b>45,000</b>	<b>100 % of \$43,500</b>
Property catastrophe, excess	<b>20,000</b>	<b>250,000</b>	<b>100 % of \$230,000</b>
Boiler and machinery	<b>N/A</b>	<b>50,000</b>	<b>100 % of \$50,000</b>

2017 Reinsurance Programs			
Type of Reinsurance	Stated Retention	Limits	Coverage
Casualty excess of loss	\$2,500	\$60,000	100 % of \$57,500
Property excess of loss	2,500	25,000	100 % of \$22,500
Surety excess of loss	1,500	45,000	100 % of \$43,500
Property catastrophe, excess	20,000	250,000	100 % of \$230,000
Boiler and machinery	N/A	50,000	100 % of \$50,000

2016 Reinsurance Programs			
Type of Reinsurance	Stated Retention	Limits	Coverage
Casualty excess of loss	\$2,500	\$40,000	100 % of \$37,500
Property excess of loss	2,500	25,000	100 % of \$22,500
Surety excess of loss	1,500	36,000	100 % of \$34,500
Property catastrophe, excess	20,000	250,000	100 % of \$230,000
Boiler and machinery	N/A	50,000	100 % of \$50,000

If we incur catastrophe losses and loss settlement expenses that exceed the coverage limits of our reinsurance program, our property catastrophe program provides one guaranteed reinstatement. In such an instance, we are required to pay the reinsurers a reinstatement premium equal to the full amount of the original premium, which will reinstate the full amount of reinsurance available under the property catastrophe program.

**Discontinued Operations - Life Insurance Business**

Premiums and losses and loss settlement expenses related to our ceded business are as follows:

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Years Ended December 31,	2018	2017	2016
<b>Ceded Business</b>			
Ceded insurance in-force	\$	—\$1,014,794	\$1,023,197
Ceded premiums earned	<b>716</b>	2,722	2,768
Loss and loss settlement expenses ceded	<b>1,473</b>	3,726	3,359

The ceding of insurance did not legally discharge United Life from primary liability under its policies. United Life must pay the loss if the reinsurer fails to meet its obligations. United Life periodically monitored the financial condition of their reinsurers to confirm that they were financially stable and had strong credit ratings. We believe that all of the reinsurers were in an acceptable financial condition.

**NOTE 5. RESERVES FOR LOSSES AND LOSS SETTLEMENT EXPENSES**

Property insurance indemnifies an insured with an interest in physical property for loss of, or damage to, such property or the loss of its income-producing abilities. Casualty insurance primarily covers liability for damage to property of, or injury to, a person or entity other than the insured. In most cases, casualty insurance also obligates the insurance company to provide a defense for the insured in litigation, arising out of events covered by the policy.

Liabilities for losses and loss settlement expenses reflect management's best estimates at a given point in time of what we expect to pay for claims that have been reported and those that have been incurred but not reported ("IBNR"), based on known facts, circumstances, and historical trends. Because property and casualty insurance reserves are estimates of the unpaid portions of incurred losses that have been reported to us, as well as losses that have been incurred but not reported, the establishment of appropriate reserves, including reserves for catastrophes, is an inherently uncertain and complex process. The ultimate cost of losses and related loss settlement expenses may vary materially from recorded amounts. We regularly update our reserve estimates as new information becomes available and as events unfold that may affect the resolution of unsettled claims. Changes in prior year reserve estimates, which may be material, are reported as a component of losses and loss settlement expenses incurred in the period such changes are determined.

The determination of reserves (particularly those relating to liability lines of insurance that have relatively longer lag in claim reporting) requires significant work to reasonably project expected future claim reporting and payment patterns. If, during the course of our regular monitoring of reserves, we determine that coverages previously written are incurring higher than expected losses, we will take action that may include, among other things, increasing the related reserves. Any adjustments we make to reserves are reflected in operating results in the year in which we make those adjustments. We engage an independent actuary, Regnier Consulting Group, Inc. ("Regnier"), to render an opinion as to the reasonableness of our statutory reserves annually. The actuarial opinion is filed in those states where we are licensed.

On a quarterly basis, United Fire's internal actuary performs a detailed actuarial review of IBNR reserves. This review includes a comparison of results from the most recent analysis of reserves completed by both our internal and external actuaries. Senior management meets with our internal actuary to review, on a regular and quarterly basis, the adequacy of carried reserves based on results from this actuarial analysis. There are two fundamental types or sources of IBNR reserves. We record IBNR reserves for "normal" types of claims and also specific IBNR reserves related to unique circumstances or events. A major hurricane is an example of an event that might necessitate establishing specific IBNR reserves because an analysis of existing historical data would not provide an appropriate estimate.

Our IBNR methodologies and assumptions are reviewed periodically, but changes are infrequent. In response to an increase in miles driven by commercial vehicles and an increase in distracted driving claims, we revised our commercial automobile severity assumptions, resulting in an increase to our carried loss IBNR. We also reviewed our

methodology and assumptions in our product liability line, associated with our construction defects business, and decreased our frequency and severity assumptions due to improvement in development patterns related to the

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statute of limitations on accident years that have matured 13 to 15 years which haven't developed to the extent we initially expected. These assumption changes resulted in a release of IBNR in 2016 and 2017 for our product liability line. Besides the changes to our assumptions used for our commercial automobile line and product liability line, we continually review and revise items affecting our projections of required reserves for unpaid loss and loss adjustment expense ("LAE"). Items reviewed and revised include development factors for paid and reported loss, paid development factors for allocated LAE, and the ratios of paid unallocated LAE to paid loss.

We do not discount loss reserves based on the time value of money.

The following table provides an analysis of changes in our property and casualty losses and loss settlement expense reserves for 2018, 2017 and 2016 (net of reinsurance amounts):

Years Ended December 31,	2018	2017	2016
Gross liability for losses and loss settlement expenses at beginning of year	\$1,224,183	\$1,123,896	\$1,003,895
Ceded losses and loss settlement expenses	(59,871 )	(59,794 )	(54,653 )
Net liability for losses and loss settlement expenses at beginning of year	\$1,164,312	\$1,064,102	\$949,242
Losses and loss settlement expenses incurred for claims occurring during			
Current year	\$785,778	\$779,966	\$683,662
Prior years	(54,167 )	(54,253 )	(31,229 )
Total incurred	\$731,611	\$725,713	\$652,433
Losses and loss settlement expense payments for claims occurring during			
Current year	\$306,032	\$311,972	\$277,053
Prior years	334,502	313,531	260,520
Total paid	\$640,534	\$625,503	\$537,573
Net liability for losses and loss settlement expenses at end of year	\$1,255,389	\$1,164,312	\$1,064,102
Ceded loss and loss settlement expenses	57,094	59,871	59,794
Gross liability for losses and loss settlement expenses at end of year	\$1,312,483	\$1,224,183	\$1,123,896

There are a multitude of factors that can impact loss reserve development. Those factors include, but are not limited to: historical data, the potential impact of various loss reserve development factors and trends including historical loss experience, legislative enactments, judicial decisions, legal developments in imposition of damages, experience with alternative dispute resolution, results of our medical bill review process, the potential impact of salvage and subrogation and changes and trends in general economic conditions, including the effects of inflation. All of these factors influence our estimates of required reserves and for long tail lines these factors can change over the course of the settlement of the claim. However, there is no precise method for evaluating the specific dollar impact of any individual factor on the development of reserves.

The significant drivers of the favorable reserve development in 2018 were our workers' compensation, reinsurance assumed, commercial automobile and fidelity and surety. During 2018 the only individual line with unfavorable development was commercial liability. Workers' compensation favorable development was primarily from reserve reductions for both reported claims and loss IBNR which were more than sufficient to offset paid loss with additional favorable development coming from loss adjustment expenses ("LAE") where the LAE IBNR reduction was more than sufficient to offset paid LAE which continues to benefit from additional litigation management efforts when compared to prior years. Reinsurance assumed favorable development is attributable reductions in reserves for both reported claims and loss IBNR as we reviewed our book of business and released excess reserves during 2018.

Commercial automobile favorable development was driven by loss adjustment expense where LAE

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IBNR reductions were more than sufficient to offset paid LAE. Fidelity and surety favorable development is attributable reductions in reserves for both reported claims and loss IBNR which were more than sufficient to offset paid loss. Commercial liability adverse development is attributable to reserve strengthening for both reported claims and loss IBNR primarily in response to an increase in umbrella auto related claims while loss adjustment expense developed favorably with reductions of LAE IBNR more than sufficient to offset paid LAE.

The significant drivers of the favorable reserve development in 2017 were our commercial liability and workers' compensation lines of business. Much of the favorable commercial liability development came from loss adjustment expense and is attributed to our continued litigation management efforts combined with some favorable development coming from decreases in reserves, which were more than sufficient to pay claims as they closed. Workers' compensation favorable development was due to the combined effects of decreases in claim reserves along with favorable changes affecting loss adjustment expense. Our personal lines also contributed favorable development. The lines that experienced adverse development during the year, which partially offset the favorable development mentioned earlier, were assumed reinsurance and commercial automobile. The adverse development for assumed reinsurance is due to increases in prior year reserves for unpaid claims while the adverse development for commercial auto is due to paid losses which were greater than reductions in reported loss reserves and reserves for claims incurred but not reported. No other single line of business contributed a significant portion of the total development.

The significant drivers of the favorable reserve development in 2016 were our commercial liability and workers' compensation lines of business. Much of the favorable commercial liability development came from loss adjustment expense and is attributed to our continued litigation management efforts. Workers' compensation favorable development was due to the combined effects of decreases in claim reserves along with favorable changes affecting loss adjustment expense. Loss adjustment expense, closely tied to loss, generally decreases when loss decreases. Commercial property, commercial automobile and assumed reinsurance lines of business exhibited adverse development which provided a partial offset to the favorable development previously noted. The adverse development for all three lines is due to paid loss which was greater than reductions in reported loss reserves and reserves for claims incurred but not reported. No other single line of business contributed a significant portion of the total development.

Generally, we base reserves for each claim on the estimated ultimate exposure for that claim. We believe that it is appropriate and reasonable to establish a best estimate for reserves within a range of reasonable estimates, especially when we are reserving for claims for bodily injury, disabilities and similar claims, for which settlements and verdicts can vary widely. Our reserving philosophy may result in favorable reserve development in future years that will decrease losses and loss settlement expenses for prior year claims in the year of adjustment. We realize that this philosophy, coupled with what we believe to be aggressive and successful claims management and loss settlement practices, has resulted in year-to-year redundancies in reserves. We believe our approach produces recorded reserves that are reasonably consistent as to their relative position within a range of reasonable reserves from year-to-year. However, conditions and trends that have affected the reserve development for a given year do change. Therefore, such development cannot be used to project future reserve redundancies or deficiencies.

We are not aware of any significant contingent liabilities related to environmental issues. Because of the type of property coverage we write, we have potential exposure to environmental pollution, mold and asbestos claims. Our underwriters are aware of these exposures and use riders or endorsements to limit exposure.

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The following tables provide information about incurred and paid losses and loss settlement expense development as of December 31, 2018, net of reinsurance, as well as cumulative development, cumulative claim frequency and IBNR liabilities. Claim data for Mercer Insurance Group, which was acquired on March 28, 2011, is presented retrospectively.

The cumulative number of reported claims, for calendar year 2018 and 2017, are counted for all lines of business on a per claimant per coverage basis and a single event may result in multiple claims due to the involvement of multiple individual claimants and / or multiple independent coverages. Claim counts for calendar years 2016 and prior are counted on a per claim and per coverage basis. Claim counts include open claims, claims that have been paid and closed, and reported claims that have been closed without the need for any payment.

**Line of business: Commercial other liability**

<b>Incurred losses and allocated loss settlement expenses, net of reinsurance</b>											<b>As of December 31, 2018</b>		
<b>For the years ended December 31,</b>													
<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>Total of incurred but not reported liabilities plus expected development on reported claims</b>	<b>Cumulative development</b>	<b>Cumulative number of reported claims</b>
	<i>(Unaudited)</i>												
<b>2009</b>	\$ 88,298	\$ 85,991	\$ 73,545	\$ 65,831	\$ 84,286	\$ 83,660	\$ 85,761	\$ 86,757	\$ 86,543	\$ 85,576	\$ 9,249	(2,722)	) 6,333
<b>2010</b>		88,987	69,533	65,299	82,865	78,564	77,948	78,291	78,498	76,956	11,859	(12,031)	) 5,264
<b>2011</b>			81,522	64,738	88,371	88,200	79,591	80,801	81,463	80,338	12,231	(1,184)	) 5,436
<b>2012</b>				100,389	96,158	94,195	91,980	92,537	91,346	89,731	15,179	(10,658)	) 5,631
<b>2013</b>					104,982	91,460	90,502	86,119	85,399	88,816	7,922	(16,166)	) 6,147
<b>2014</b>						118,928	117,958	106,486	97,809	102,487	10,092	(16,441)	) 6,289
<b>2015</b>							137,386	125,307	120,005	127,091	19,976	(10,295)	) 7,385
<b>2016</b>								139,144	130,041	136,275	26,097	(2,869)	) 8,217
<b>2017</b>									139,602	139,032	38,919	(570)	) 7,837
<b>2018</b>										163,059	78,705		6,088
										<b>Total</b>	<b>\$ 1,089,361</b>		

Table of Contents**Line of business: Commercial other liability****Cumulative paid losses and allocated loss settlement expenses, net of reinsurance****For the years ended December 31,**

<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
	<i>(Unaudited)</i>									
<b>2009</b>	\$ 8,375	\$ 21,151	\$ 32,073	\$ 41,696	\$ 50,098	\$ 56,789	\$ 63,149	\$ 67,733	\$ 70,814	\$ 72,673
<b>2010</b>		7,103	15,230	24,577	35,043	51,336	56,761	60,116	62,070	63,300
<b>2011</b>			6,236	13,670	26,260	40,595	50,146	56,150	62,165	64,541
<b>2012</b>				6,875	24,620	39,948	55,316	64,574	69,800	71,773
<b>2013</b>					9,835	25,228	39,953	54,559	65,773	72,115
<b>2014</b>						10,207	29,679	50,211	70,363	83,109
<b>2015</b>							11,185	27,182	53,901	74,292
<b>2016</b>								13,782	38,184	63,526
<b>2017</b>									17,716	43,172
<b>2018</b>										16,200
									<b>Total</b>	<b>\$ 624,701</b>
										All outstanding liabilities for unpaid losses and loss settlement expenses before 2009, net of reinsurance
										31,672
										Liabilities for unpaid losses and loss settlement expenses, net of reinsurance
										\$ 496,332

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## Line of business: Commercial fire and allied

Incurred losses and allocated loss settlement expenses, net of reinsurance										As of December 31, 2018		
For the years ended December 31,										Total of incurred but not reported liabilities plus expected development on reported claims	Cumulative development reported claims	
Accident Year	2009	2010	2011	2012	2013	2014	2015	2016	2017			2018
	<i>(Unaudited)</i>											
2009	\$ 113,754	\$ 106,085	\$ 105,031	\$ 105,614	\$ 87,751	\$ 87,845	\$ 87,932	\$ 88,891	\$ 89,027	\$ 88,648	\$ 80(25,106	) 18,053
2010		113,139	106,152	108,246	83,836	83,932	83,767	83,981	84,213	84,123	65 (29,016	) 16,690
2011			148,220	142,330	117,082	120,492	119,820	120,219	121,434	121,319	281 (26,901	) 16,037
2012				138,602	110,448	108,774	108,047	107,958	108,623	109,687	813 (28,915	) 6,438
2013					91,521	88,550	91,498	92,212	93,826	93,858	515 2,337	6,626
2014						126,216	131,198	128,762	128,185	128,503	1,012,287	7,883
2015							103,177	108,293	110,633	108,235	1,633,058	7,523
2016								147,473	144,208	143,721	2,320,752	) 9,703
2017									155,139	160,240	4,553,101	13,021
2018										143,280	13,286	9,235
										Total	\$ 1,181,614	

Table of Contents**Line of business: Commercial fire and allied****Cumulative paid losses and allocated loss settlement expenses, net of reinsurance****For the years ended December 31,**

Accident Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
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*(Unaudited)*

<b>2009</b>	\$53,219	\$72,181	\$77,732	\$82,809	\$86,930	\$87,544	\$87,721	\$88,037	\$88,159	\$88,334
<b>2010</b>		52,660	72,271	78,284	80,352	82,037	83,000	83,374	83,915	83,942
<b>2011</b>			85,585	104,800	109,429	112,497	116,614	118,183	120,178	120,731
<b>2012</b>				71,008	94,380	100,078	103,197	105,250	106,521	106,740
<b>2013</b>					59,331	78,226	82,853	86,115	89,200	91,493
<b>2014</b>						84,456	113,663	116,750	122,370	123,697
<b>2015</b>							67,217	90,454	95,515	101,367
<b>2016</b>								92,895	125,962	132,429
<b>2017</b>									99,484	137,058
<b>2018</b>										92,770
									Total	\$1,078,561
										All outstanding liabilities for unpaid losses and loss settlement expenses before 2009, net of reinsurance
										522
										Liabilities for unpaid losses and loss settlement expenses, net of reinsurance
										\$103,575

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**Line of business: Commercial automobile**

<b>Incurred losses and allocated loss settlement expenses, net of reinsurance</b>											<b>As of December 31, 2018</b>	
<b>For the years ended December 31,</b>											<b>Total of incurred but not reported liabilities plus expected development on reported claims</b>	<b>Cumulative number of reported claims</b>
<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>		
	<i>(Unaudited)</i>											
<b>2009</b>	\$ 80,021	\$ 69,328	\$ 68,569	\$ 64,121	\$ 64,516	\$ 63,605	\$ 63,560	\$ 63,567	\$ 63,509	\$ 63,506	\$ (46,515)	) 15,019
<b>2010</b>		75,781	68,068	65,860	67,015	67,563	67,296	68,086	67,910	67,893	5 (7,888)	) 16,246
<b>2011</b>			84,887	87,299	90,750	92,519	92,379	91,336	90,766	90,838	199,951	) 15,248
<b>2012</b>				100,039	90,848	94,755	95,321	96,594	96,389	96,305	243,734	) 14,364
<b>2013</b>					104,356	98,037	102,943	103,726	104,980	105,248	8892	) 15,520
<b>2014</b>						107,723	106,076	113,720	118,869	120,385	1,706,662	) 17,277
<b>2015</b>							125,506	129,816	132,206	138,987	3,837,481	) 19,961
<b>2016</b>								174,018	175,357	174,337	10,793	) 27,040
<b>2017</b>									227,919	224,553	28,3966	) 32,281
<b>2018</b>										236,629	65,079	) 30,521
										<b>Total</b>	<b>\$ 1,318,681</b>	

Table of Contents**Line of business: Commercial automobile****Cumulative paid losses and allocated loss settlement expenses, net of reinsurance****For the years ended December 31,**

<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
	<i>(Unaudited)</i>									
<b>2009</b>	\$27,674	\$44,867	\$53,451	\$58,087	\$61,398	\$62,732	\$63,495	\$63,503	\$63,508	\$63,506
<b>2010</b>		29,329	41,141	52,953	57,947	62,231	65,169	67,622	67,852	67,853
<b>2011</b>			34,332	50,931	65,021	79,383	85,348	87,475	88,609	89,459
<b>2012</b>				39,247	57,201	71,469	82,944	90,292	93,179	94,747
<b>2013</b>					43,592	67,630	79,663	90,780	96,375	100,058
<b>2014</b>						45,704	68,033	87,590	99,922	109,682
<b>2015</b>							50,782	78,225	99,201	118,395
<b>2016</b>								66,013	103,528	128,157
<b>2017</b>									81,311	126,644
<b>2018</b>										81,572
									<b>Total</b>	<b>\$980,073</b>
										All outstanding liabilities for unpaid losses and loss settlement expenses before 2009, net of reinsurance
										56
										Liabilities for unpaid losses and loss settlement expenses, net of reinsurance
										\$338,664

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Line of business: Workers' compensation

Incurred losses and allocated loss settlement expenses, net of reinsurance											As of December 31, 2018		
For the years ended December 31,											Total of incurred but not reported liabilities plus expected development on reported claims	Cumulative development	Cumulative number of reported claims
Accident Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018			
	<i>(Unaudited)</i>												
2009	\$43,560	\$39,009	\$36,294	\$36,837	\$36,823	\$36,158	\$36,014	\$35,026	\$35,012	\$34,783	\$193	(8,777	) 4,265
2010		38,210	42,531	41,180	41,167	40,647	41,422	41,468	42,617	42,666	346	4,456	) 3,986
2011			39,967	38,481	35,352	34,309	33,585	33,314	33,352	32,707	425	(7,260	) 3,955
2012				48,848	46,279	42,158	38,423	38,553	39,015	39,182	503	(9,666	) 3,982
2013					64,048	62,579	56,369	54,584	52,761	51,753	781	(12,295	) 4,236
2014						64,051	60,729	58,284	56,630	54,636	1,106	(9,415	) 4,668
2015							53,788	55,578	51,003	46,682	935	(7,106	) 5,515
2016								70,419	66,575	61,648	2,042	(8,771	) 7,376
2017									76,184	69,528	3,744	(6,656	) 7,283
2018										71,972	5,885		) 5,478
										Total	\$505,557		



Table of Contents**Line of business: Workers' compensation****Cumulative paid losses and allocated loss settlement expenses, net of reinsurance****For the years ended December 31,**

<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
	<i>(Unaudited)</i>									
<b>2009</b>	\$ 10,478	\$ 20,292	\$ 24,189	\$ 27,747	\$ 29,898	\$ 31,003	\$ 31,886	\$ 32,911	\$ 33,117	\$ 33,313
<b>2010</b>		11,821	22,606	28,765	31,887	33,119	34,143	35,052	38,973	39,208
<b>2011</b>			10,322	21,678	26,033	27,497	28,247	29,022	29,453	29,700
<b>2012</b>				11,802	23,023	28,397	30,933	33,063	34,330	35,388
<b>2013</b>					14,136	30,209	38,023	42,941	45,078	47,071
<b>2014</b>						13,965	30,289	38,441	42,964	45,193
<b>2015</b>							12,063	27,304	35,229	38,424
<b>2016</b>								14,413	32,345	40,680
<b>2017</b>									14,647	31,309
<b>2018</b>										16,949
									<b>Total</b>	<b>\$ 357,235</b>
										All outstanding liabilities for unpaid losses and loss settlement expenses before 2009, net of reinsurance
										20,232
										Liabilities for unpaid losses and loss settlement expenses, net of reinsurance
										\$ 168,554

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Line of business: Personal

Incurred losses and allocated loss settlement expenses, net of reinsurance											As of December 31, 2018	
For the years ended December 31,											Total	
Accident Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	of incurred but not reported liabilities plus expected development on reported claims	Cumulative number of reported claims
	<i>(Unaudited)</i>											
2009	\$ 34,597	\$ 33,519	\$ 31,945	\$ 32,026	\$ 32,134	\$ 32,029	\$ 32,085	\$ 32,070	\$ 31,867	\$ 31,879	\$ 2(2,718	) 13,502
2010		36,686	34,347	33,928	33,865	33,403	33,413	33,432	33,213	33,204	14(3,482	) 13,330
2011			50,014	48,534	47,090	47,035	46,968	47,013	46,733	46,761	32(3,253	) 14,846
2012				47,924	46,199	46,403	46,150	44,715	44,352	44,165	7(3,759	) 10,776
2013					39,232	38,525	37,262	37,086	36,729	36,661	36(2,571	) 9,240
2014						53,910	52,661	52,944	52,782	52,615	76(1,295	) 10,929
2015							42,848	41,088	40,336	40,368	132(2,480	) 9,522
2016								48,072	45,840	45,379	351(2,693	) 11,840
2017									60,330	59,342	733(988	) 14,454
2018										51,639	3,027	12,246
									Total	\$ 442,013		

Table of Contents**Line of business: Personal****Cumulative paid losses and allocated loss settlement expenses, net of reinsurance  
For the years ended December 31,**

<b>Accident Year</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
	<i>(Unaudited)</i>									
<b>2009</b>	\$22,086	\$27,926	\$29,801	\$30,829	\$31,564	\$31,644	\$31,718	\$31,804	\$31,837	\$31,849
<b>2010</b>		24,499	29,867	31,340	32,076	32,771	32,997	33,165	33,158	33,154
<b>2011</b>			36,489	43,801	45,306	45,949	46,487	46,573	46,575	46,650
<b>2012</b>				30,415	41,979	43,375	44,448	43,569	44,139	44,158
<b>2013</b>					25,505	32,788	34,297	35,306	36,155	36,323
<b>2014</b>						37,055	47,912	49,710	51,837	52,018
<b>2015</b>							29,551	37,431	39,027	39,428
<b>2016</b>								32,999	40,910	42,660
<b>2017</b>									42,135	53,111
<b>2018</b>										37,410
									<b>Total</b>	<b>\$416,761</b>
										All outstanding liabilities for unpaid losses and loss settlement expenses before 2009, net of reinsurance
										1,418
										Liabilities for unpaid losses and loss settlement expenses, net of reinsurance
										\$26,668

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The reconciliation of the net incurred and loss development tables to the liability for unpaid losses and loss settlement expenses in the consolidated statement of financial position is as follows.

	December 31, 2018
Net outstanding liabilities for unpaid losses and allocated loss settlement expenses:	
Commercial other liability	\$ 496,332
Commercial fire and allied	103,575
Commercial automobile	338,664
Commercial workers' compensation	168,554
Personal	26,668
All other lines	32,595
Net outstanding liabilities for unpaid losses and allocated loss settlement expenses	1,166,388
Net outstanding liabilities for unpaid unallocated loss settlement expenses	86,753
Fair value adjustment (purchase accounting adjustment for Mercer acquisition)	2,248
Liabilities for unpaid losses and loss settlement expenses, net of reinsurance	1,255,389
Reinsurance recoverable on unpaid losses and allocated loss settlement expenses:	
Commercial other liability	22,556
Commercial fire and allied	2,723
Commercial automobile	3,166
Commercial workers' compensation	27,465
Personal	4
All other lines	3,329
Reinsurance recoverable on unpaid losses and allocated loss settlement expenses	59,243
Reinsurance fair value amortization (purchase accounting adjustment for Mercer acquisition)	(2,149 )
Total reinsurance recoverable on unpaid losses and loss settlement expenses	57,094
Total gross liability for unpaid losses and loss settlement expenses	\$ 1,312,483

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**Average annual percentage payout of incurred claims by  
age, net of reinsurance**

	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>	<b>Year 6</b>	<b>Year 7</b>	<b>Year 8</b>	<b>Year 9</b>	<b>Year 10</b>
	<i>(Unaudited)</i>									
Commercial other liability	9.7 %	15.5 %	16.7 %	16.0 %	13.0 %	7.1 %	5.4 %	3.6 %	2.6 %	2.2 %
Commercial fire and allied	64.0 %	21.4 %	4.9 %	3.8 %	2.7 %	1.3 %	0.6 %	0.5 %	0.1 %	0.2 %
Commercial automobile	39.0 %	20.5 %	14.8 %	11.0 %	6.5 %	3.1 %	1.9 %	0.4 %	— %	— %
Commercial workers' compensation	26.6 %	29.3 %	14.1 %	7.6 %	4.2 %	3.0 %	2.2 %	4.3 %	0.6 %	0.6 %
Personal	71.9 %	19.1 %	4.0 %	2.4 %	1.0 %	0.6 %	0.2 %	0.1 %	— %	— %

Table of Contents**NOTE 6. STATUTORY REPORTING, CAPITAL REQUIREMENTS AND DIVIDENDS AND RETAINED EARNINGS RESTRICTIONS**

Statutory capital and surplus in regards to policyholders at December 31, 2018, 2017 and 2016 and statutory net income (loss) for the years then ended are as follows:

	Statutory Capital and Surplus	Statutory Net Income (Loss)
<b>2018</b>		
<b>Property and casualty business</b>	<b>\$ 774,257</b>	<b>\$ 219,065</b>
<b>Life, accident and health business<sup>(1)</sup></b>	<b>—</b>	<b>3,548</b>
<b>2017</b>		
Property and casualty business	\$ 757,443	\$ 19,687
Life, accident and health business	144,533	5,485
<b>2016</b>		
Property and casualty business	\$ 770,908	\$ 39,087
Life, accident and health business	139,806	(3,177 )

The 2018 Life, accident and health business only includes results prior to the closing of the sale of United Life Insurance Company, which closed on March 30, 2018. Prior to the closing of the sale, United Fire & Casualty Company owned United Life Insurance Company, accordingly, the property and casualty  
(1) statutory capital and surplus includes life, accident and health statutory capital and surplus, and therefore represents our total consolidated statutory capital and surplus.

State insurance holding company laws and regulations generally require approval from the insurer's domicile state insurance Commissioner for any material transaction or extraordinary dividend. For property and casualty insurers, a material transaction is defined as any sale, loan, exchange, transfer or guarantee with an affiliate where the aggregate value of the transaction exceeds 25 percent of the insurer's policyholders' surplus or three percent of its admitted assets (measured at December 31 of the preceding year), whichever is less. For life insurers, a material transaction with an affiliate is defined as a transaction with an aggregate value exceeding three percent of the life insurer's admitted assets (measured at December 31 of the preceding year).

State laws and regulations generally limit the amount of funds that an insurance company may distribute to a parent as a dividend without Commissioner approval. As a holding company with no independent operations of its own, United Fire Group, Inc. relies on dividends received from its insurance company subsidiaries in order to pay dividends to its common shareholders. Dividends payable by our insurance subsidiaries are governed by the laws in the states in which they are domiciled. In all cases, these state laws permit the payment of dividends only from earned surplus arising from business operations. For example, under Iowa law, the maximum dividend or distribution that may be paid within a 12-month period without prior approval of the Iowa Insurance Commissioner is generally restricted to the greater of 10 percent of statutory surplus as of the preceding December 31, or net income of the preceding calendar year on a statutory basis, not greater than earned statutory surplus. Other states in which our insurance company subsidiaries are domiciled may impose similar restrictions on dividends and distributions. Based on these restrictions, at December 31, 2018, our insurance company subsidiary, United Fire & Casualty, is able to make a minimum of \$106.2 million in dividend payments without prior regulatory approval. At December 31, 2018, we were in compliance with applicable state laws and regulations. These restrictions will not have a material impact in meeting our cash obligations. In addition, United Fire Group, Inc. maintains a credit agreement, as discussed in Note 14 "Credit Facility," which permits us to borrow up to an aggregate principal amount of \$50,000 and allows the Company to increase the aggregate amount of the commitments thereunder by up to \$100,000.

We paid dividends to our common shareholders of \$105,408, \$27,337 and \$24,591 in 2018, 2017 and 2016, respectively. Payments of any future dividends and the amounts of such dividends, however, will depend upon factors such as net income, financial condition, capital requirements, and general business conditions. We will only pay dividends if declared by our Board of Directors, out of funds legally available, and subject to any other restrictions that may be applicable to us.



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In 2018, 2017 and 2016, United Fire & Casualty Company received dividends from its wholly owned subsidiaries of \$8,500, \$13,300 and \$26,000, respectively. In 2018, 2017 and 2016, United Fire & Casualty Company paid dividends to United Fire Group, Inc. totaling \$105,000, \$40,000 and \$24,000, respectively. These intercompany dividend payments are eliminated for reporting in our Consolidated Financial Statements.

Our property and casualty subsidiaries are required to prepare and file statutory-basis financial statements in conformity with the National Association of Insurance Commissioners ("NAIC") Accounting Practices and Procedures Manual, subject to any deviations prescribed or permitted by the applicable insurance commissioner and/or director. The accounting principles used to prepare these statutory-basis financial statements follow prescribed or permitted accounting practices that differ from GAAP. Prescribed statutory accounting principles include state laws, regulations and general administrative rules issued by the state of domicile, as well as a variety of publications and manuals of the NAIC. Permitted accounting practices encompass all accounting practices not prescribed, but allowed by the state of domicile. No material permitted accounting practices were used to prepare our statutory-basis financial statements during 2018, 2017 and 2016. Statutory accounting principles primarily differ from GAAP in that policy acquisition and certain sales inducement costs are charged to expense as incurred, goodwill is amortized, life insurance reserves are established based on different actuarial assumptions and the values reported for investments, pension obligations and deferred taxes are established on a different basis.

We are directed by the state insurance departments' solvency regulations to calculate a required minimum level of statutory capital and surplus based on insurance risk factors. The risk-based capital results are used by the NAIC and state insurance departments to identify companies that merit regulatory attention or the initiation of regulatory action. United Fire & Casualty Company and its property and casualty insurance subsidiaries and affiliates had statutory capital and surplus in regards to policyholders well in excess of their required levels at December 31, 2018.

**NOTE 7. FEDERAL INCOME TAX**

The Tax Act was enacted on December 22, 2017. The Tax Act significantly revised the U.S. corporate income tax laws including lowering the U.S. federal corporate tax rate from 35 percent to 21 percent, effective January 1, 2018.

In December 2017, the SEC staff issued Staff Accounting Bulletin No. 118, which addresses how a company recognizes provisional amounts when a company does not have the necessary information available, prepared or analyzed in reasonable detail to complete its accounting for the effect of the changes in the Tax Act. The measurement period ends when a company has obtained, prepared and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. As of December 31, 2018 we have completed accounting for the tax effects of enactment of the Tax Act and no adjustments were made during the measurement period.

Federal income tax expense (benefit) from both continuing and discontinued operations is composed of the following:

Years Ended December 31, <b>2018</b>	2017	2016	
Current	<b>\$18,493</b>	\$1,989	\$3,239
Deferred	<b>(21,791 )</b>	(26,719 )	5,524
Total	<b>\$(3,298 )</b>	\$(24,730 )	\$8,763



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A reconciliation of income tax expense (benefit) computed at the applicable federal tax rate of 21.0 percent in 2018 and 35.0 percent in 2017 to the amount recorded in the accompanying Consolidated Statements of Income and Comprehensive Income is as follows:

Years Ended December 31,	<b>2018</b>	2017	2016
Computed expected income tax expense	<b>\$5,114</b>	\$9,202	\$20,533
Impact of enactment of Tax Act	—	(21,884 )	—
Tax-exempt municipal bond interest income	<b>(4,235 )</b>	(8,875 )	(8,330 )
Nontaxable dividend income	<b>(591 )</b>	(1,540 )	(1,317 )
Valuation allowance reduction	<b>(329 )</b>	(547 )	(547 )
Other, net	<b>(3,257 )</b>	(1,086 )	(1,576 )
Consolidated federal income tax expense (benefit)	<b>\$(3,298 )</b>	\$(24,730 )	\$8,763
Reconciliation of consolidated federal income tax expense (benefit) from:			
Continuing operations	<b>\$(11,405 )</b>	\$(29,220 )	\$8,379
Gain on sale of discontinued operations	<b>7,544</b>	—	—
Discontinued operations	<b>563</b>	4,490	384
Consolidated federal income tax expense (benefit)	<b>\$(3,298 )</b>	\$(24,730 )	\$8,763

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We measure certain deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is 21.0 percent. The significant components of our net deferred tax liability at December 31, 2018 and 2017 are as follows:

December 31,	2018	2017
Deferred tax liabilities		
Net unrealized appreciation on investment securities:		
Equity securities	\$38,430	\$50,839
All other securities	(2,478 )	7,599
Deferred policy acquisition costs	19,487	30,404
Investments in partnerships	2,510	3,653
Prepaid pension cost	4,158	3,416
Net bond discount accretion	296	666
Depreciation	1,063	593
Revaluation of investment basis <sup>(1)</sup>	419	545
Identifiable intangible assets <sup>(1)</sup>	1,689	1,838
Other	1,639	1,934
Gross deferred tax liability	\$67,213	\$101,487
Deferred tax assets		
Financial statement reserves in excess of income tax reserves	\$19,800	\$17,036
Unearned premium adjustment	20,406	19,389
Net operating loss carryforwards	—	329
Underfunded benefit plan obligation	5,622	12,375
Post-retirement benefits other than pensions	12,035	11,942
Other-than-temporary impairment of investments	2,094	2,313
Contingent ceding commission accrual	14	317
Alternative minimum tax credit carryforward	—	6,011
Compensation expense related to stock options	3,506	3,289
Other	4,648	4,145
Gross deferred tax asset	\$68,125	\$77,146
Valuation allowance	—	(329 )
Deferred tax asset	\$68,125	\$76,817
Net deferred tax liability (asset)	\$(912 )	\$24,670

(1) Related to our acquisition of Mercer Insurance Group.

Due to our determination that we may not be able to fully realize the benefits of the net operating losses ("NOLs") acquired in the purchase of American Indemnity Financial Corporation in 1999, which are only available to offset the future taxable income of our property and casualty insurance operations and are further limited as to the amount that can be utilized in any given year, we did not record a valuation allowance against these NOLs at December 31, 2018. At December 31, 2017 we recorded a valuation allowance against these NOLs of \$329. Based on a yearly review, we determine whether the benefit of the NOLs can be realized, and, if so, the decrease in the valuation allowance is recorded as a reduction to current federal income tax expense. If NOLs expire during the year, the decrease in the valuation allowance is offset with a corresponding decrease to the deferred income tax asset. The valuation allowance was reduced by \$657 during 2018 due to the realization of \$3,129 in NOLs. The valuation allowance was reduced by \$547 in 2017 due to no realization of NOLs. At December 31, 2018, there are no remaining NOL's. At December 31, 2018, we had no alternative minimum tax credit carryforwards.



Table of Contents**NOTE 8. EMPLOYEE BENEFITS**

We offer various benefits to our employees including a noncontributory defined benefit pension plan, an employee/retiree health and dental benefit plan, a profit-sharing plan and an employee stock ownership plan.

**Pension and Post-retirement Benefit Plans**

We offer a noncontributory defined benefit pension plan in which all of our employees are eligible to participate after they have completed one year of service, attained 21 years of age and have met the hourly service requirements.

Retirement benefits under our pension plan are based on the number of years of service and level of compensation. Our policy to fund the pension plan on a current basis is to not less than the minimum amounts required by the Employee Retirement Income Security Act of 1974, as amended, and the Internal Revenue Code of 1986, as amended, is to assure that plan assets will be adequate to provide retirement benefits. We estimate that we will contribute approximately \$4,000 to the pension plan in 2019.

We also offer a health and dental benefit plan to all of our eligible employees and retirees that consists of two programs: (1) the self-funded employee health and dental benefit plan and (2) the self-funded (pre-65) and fully-funded (post-65) retiree health and dental benefit plan (the "post-retirement benefit plan"). Effective January 1, 2017, there was a plan amendment, which included the following changes: eliminated the pre-65 retirement plan with a \$500 hundred dollar deductible; for retirements after January 1, 2017, the retiree will pay 50 percent of the lower cost supplemental plan if they are 65 or older and 100 percent of the premium if less than 65; and removed spousal coverage after the death of the participant. The financial impact of the changes were reflected in accumulated other comprehensive income at December 31, 2016. Effective January 1, 2019, there was a plan amendment, which requires spouses to pay 100 percent of the medical, dental & vision premiums and the subsidy for the post-65 retirees is based off the lowest cost Medicare Supplement Plan (Plan 1). The financial impact of the changes were reflected in accumulated other comprehensive income at December 31, 2018.

The post-retirement benefit plan provides health and dental benefits to our retirees (and covered dependents) who have met the service and participation requirements stipulated by the post-retirement benefit plan. The third party administrators for the post-retirement benefit plan are responsible for making medical and dental care benefit payments. Participants are required to submit claims for reimbursement or payment to the claims administrator within twelve months after the end of the calendar year in which the charges were incurred. An unfunded benefit obligation is reported for the post-retirement benefit plan in the accompanying Consolidated Balance Sheets.

**Investment Policies and Strategies**

Our investment policy and objective for the pension plan is to generate long-term capital growth and income by way of a diversified investment portfolio along with appropriate employer contributions, which will allow us to provide for the pension plan's benefit obligation.

The investments held by the pension plan at December 31, 2018 include the following asset categories:

• Fixed income securities, which may include bonds, and convertible securities;

• Equity securities, which may include various types of stock, such as large-cap, mid-cap, small-cap, and international stocks;

• Pooled separate accounts, which includes two separate funds, a core plus bond separate account and a real estate separate account;

• An arbitrage fund, which is a fund that takes advantage of price discrepancies, primarily equity securities, for the same asset in different markets;

• A group annuity contract that is administered by United Life, a former subsidiary of United Fire; and

• Cash and cash equivalents, which include money market funds.

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We have an internal investment/retirement committee, which includes our Chief Executive Officer, Chief Investment Officer, and Chief Operating Officer, all of whom receive monthly information on the value of the pension plan assets and their performance. Quarterly, the committee meets to review and discuss the performance of the pension plan assets as well as the allocation of investments within the pension plan.

As of December 31, 2018, we had six external investment managers that are allowed to exercise investment discretion, subject to limitations, if any, established by the investment/retirement committee. We utilize multiple investment managers in order to maximize the pension plan's investment return while mitigating risk. None of our investment managers uses leverage in managing the pension plan. Annually, the investment/retirement committee meets with each investment manager to review the investment manager's goals, objectives and the performance of the assets they manage. The decision to establish or terminate a relationship with an investment manager is at the discretion of our investment/retirement committee.

We consider historical experience for comparable investments and the target allocations we have established for the various asset categories of the pension plan to determine the expected long-term rate of return, which is an assumption as to the average rate of earnings expected on the pension plan funds invested, or to be invested, by the pension plan, to provide for the settlement of benefits included in the projected pension benefit obligation. Investment securities, in general, are exposed to various risks, such as fluctuating interest rates, credit standing of the issuer of the security and overall market volatility. Annually, we perform an analysis of expected long-term rates of return based on the composition and allocation of our pension plan assets and recent economic conditions.

The following is a summary of the pension plan's actual and target asset allocations at December 31, 2018 and 2017 by asset category:

Pension Plan Assets	2018	% of Total	2017	% of Total	Target
					Allocation
Fixed maturity securities - corporate bonds	\$10,051	6.1 %	\$11,003	7.0 %	0 % - 15 %
Redeemable preferred stock	2,697	1.6 %	3,216	2.0 %	0 % - 10 %
Equity securities	86,586	52.5 %	87,603	55.6 %	50 % - 70 %
Pooled separate accounts					
Core plus bond separate account fund	20,222	12.3 %	17,948	11.4 %	0 % - 40 %
U.S. property separate account fund	20,841	12.6 %	15,502	9.8 %	0 % - 25 %
Arbitrage fund	8,716	5.3 %	8,506	5.4 %	0 % - 10 %
United Life annuity	10,339	6.3 %	9,846	6.2 %	5 % - 10 %
Cash and cash equivalents	5,367	3.3 %	4,020	2.6 %	0 % - 10 %
Total plan assets	\$164,819	100.0 %	\$157,644	100.0 %	

The investment return expectations for the pension plan are used to develop the asset allocation based on the specific needs of the pension plan. Accordingly, equity securities comprise the largest portion of our pension plan assets, as they yield the highest rate of return. The United Life annuity, which is the fifth largest asset category and was originally written by our former life insurance subsidiary in 1976, provides a guaranteed rate of return. The interest rate on the group annuity contract is determined annually.

The availability of assets held in cash and cash equivalents enables the pension plan to mitigate market risk that is associated with other types of investments and allows the pension plan to maintain liquidity both for the purpose of making future benefit payments to participants and their beneficiaries and for future investment opportunities.

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**Valuation of Investments**

***Fixed Maturity and Equity Securities***

Investments in equity securities are stated at fair value based upon quoted market prices reported on recognized securities exchanges on the last business day of the year. Purchases and sales of securities are recorded as of the trade date.

The fair value of fixed maturity securities categorized as Level 2 is determined by management based on fair value information reported in the custodial statements received from Plan's investment managers, which is derived from recent trading activity of the underlying security in the financial markets. These securities represent various taxable bonds held by the pension plan. These securities categorized as Level 2 are valued in the same manner as described in Part II, Item 8, Note 3 and have the same controls in place.

***Pooled Separate Accounts***

The pension plan invests in two pooled separate account funds, a core plus bond separate account fund and a U.S. property separate account fund. Investments in the core plus bond separate account fund are stated at fair value as provided by the administrator of the fund based on the fair value of the underlying assets owned by the fund. The fair value measurement is classified within Level 2 of the fair value hierarchy. The fair value of the investments in the U.S. property separate account fund is provided by the administrator of the fund based on the net asset value of the fund. The net asset value is based on the fair value of the underlying properties included in the fund. The fair value of the underlying properties are based on property appraisals conducted by an independent third party. The fair value measurement is classified within Level 3 of the fair value hierarchy. We have not adjusted the net asset value provided by the custodian for either fund.

***Arbitrage Fund***

The fair value of the arbitrage fund is determined based on its net asset value, which is obtained from the custodian and determined monthly with issuances and redemptions of units of the fund made, based on the net asset value per unit as determined on the valuation date. We have not adjusted the net asset value provided by the custodian.

***United Life Annuity***

The United Life group annuity contract, which is a deposit administration contract, is stated at contract value as determined by United Life. Under the group annuity contract, the plan's investment account is credited with compound interest on the average account balance for the year. The interest rate is equivalent to the ratio of net investment income to mean assets of United Life, net of investment expenses.

***Cash and Cash Equivalents***

Cash and cash equivalents primarily consist of insured cash and money market funds held with various financial institutions. Interest is earned on a daily basis. The fair value of these funds approximates their cost basis due to their short-term nature.

**Fair Value Measurement**

The following tables present the categorization of the pension plan's assets measured at fair value on a recurring basis at December 31, 2018 and 2017:

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Description	December 31, 2018	Fair Value Measurements		
		Level 1	Level 2	Level 3
Fixed maturity securities - corporate bonds	\$ 10,051	\$—	\$10,051	\$—
Redeemable preferred stock	2,697	2,697	—	—
Equity securities	86,586	86,586	—	—
Pooled separate accounts				
Core plus bond separate account fund	20,222	—	20,222	—
U.S. property separate account fund	20,841	—	—	20,841
Arbitrage fund	8,716	—	8,716	—
Money market funds	5,364	5,364	—	—
Total assets measured at fair value	\$ 154,477	\$94,647	\$38,989	\$20,841

Description	December 31, 2017	Fair Value Measurements		
		Level 1	Level 2	Level 3
Fixed maturity securities - corporate bonds	\$ 11,003	\$—	\$11,003	\$—
Redeemable preferred stock	3,216	3,216	—	—
Equity securities	87,603	87,603	—	—
Pooled separate accounts				
Core plus bond separate account fund	17,948	—	17,948	—
U.S. property separate account fund	15,502	—	—	15,502
Arbitrage fund	8,506	—	8,506	—
Money market funds	4,011	4,011	—	—
Total assets measured at fair value	\$ 147,789	\$94,830	\$37,457	\$15,502

There were no transfers of assets in or out of Level 1 or Level 2 during the period.

The fair value of investments categorized as Level 1 is based on quoted market prices that are readily and regularly available.

The fair value of fixed maturity securities categorized as Level 2 is determined by management based on fair value information reported in the custodial statements, which is derived from recent trading activity of the underlying security in the financial markets. These securities represent various taxable bonds held by the pension plan. These securities categorized as Level 2 are valued in the same manner as described in Part II, Item 8, Note 3 and have the same controls in place.

The fair value of the arbitrage fund and bond and mortgage pooled separate account fund are categorized as Level 2 since there are no restrictions as to the pension plan's ability to redeem its investment at the net asset value of the fund as of the reporting date.

The following tables provide a summary of the changes in fair value of the pension plan's Level 3 securities:

	U.S. property separate account fund
Balance at January 1, 2018	\$ 15,502
Unrealized gains	1,339
Company Contributions	4,000
Balance at December 31, 2018	\$ 20,841





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	U.S. property separate account fund
Balance at January 1, 2017	\$ 14,330
Unrealized gains	1,172
Balance at December 31, 2017	\$ 15,502

**Estimates and Assumptions**

The preparation of financial statements in conformity with GAAP requires us to make various estimates and assumptions that affect the reporting of net periodic benefit cost, plan assets and plan obligations for each plan at the date of the financial statements. Actual results could differ from these estimates. One significant estimate relates to the calculation of the benefit obligation for each plan. We annually establish the discount rate, which is an estimate of the interest rate at which these benefits could be effectively settled, that is used to determine the present value of the respective plan's benefit obligations as of December 31. In estimating the discount rate, we look to rates of return on high-quality, fixed-income investments currently available and expected to be available during the period to maturity of the respective plan's benefit obligations.

In October 2014, the Society of Actuaries finalized a new mortality table and a new mortality improvement scale. The mortality improvement scale was further refined by the Society of Actuaries in 2015, 2016 and 2017. In October 2018, the mortality assumption has been updated to reflect the annual historical U.S. mortality data to 2016 published by the Society of Actuaries. These updated tables reflect improved life expectancies and an expectation that the trend will continue. We have reviewed these updated tables and have updated the mortality assumptions based on this information and also based on research provided by our external actuaries. We will continue to monitor mortality assumptions and make changes as appropriate to reflect additional research and our resulting best estimate of future mortality rates.

***Assumptions Used to Determine Benefit Obligations***

The following actuarial assumptions were used to determine the reported plan benefit obligations at December 31:

Weighted-average assumptions as of	Pension Benefits		Post-retirement Benefits	
	2018	2017	2018	2017
December 31,	<b>2018</b>	2017	<b>2018</b>	2017
Discount rate	<b>4.18 %</b>	3.65 %	<b>4.18 %</b>	3.65 %
Rate of compensation increase	<b>3.00</b>	3.00	<b>N/A</b>	N/A

Increasing interest rates resulted in an increase in the discount rates we use to value our respective plan's benefit obligations at December 31, 2018 compared to December 31, 2017.

***Assumptions Used to Determine Net Periodic Benefit Cost***

The following actuarial assumptions were used at January 1 to determine our reported net periodic benefit costs for the year ended December 31:

Weighted-average assumptions as of	Pension Benefits			Post-retirement Benefits		
	2018	2017	2016	2018	2017	2016
January 1,	<b>2018</b>	2017	2016	<b>2018</b>	2017	2016
Discount rate	<b>3.65 %</b>	4.17 %	4.21 %	<b>3.65 %</b>	4.17 %	4.21 %
Expected long-term rate of return on plan assets	<b>6.70</b>	7.50	7.50	<b>N/A</b>	N/A	N/A
Rate of compensation increase	<b>3.00</b>	3.00	3.00	<b>N/A</b>	N/A	N/A



Table of Contents**Assumed Health Care Cost Trend Rates**

Years Ended December 31,	Health Care Benefits		Dental Claims	
	2018	2017	2018	2017
Health care cost trend rates assumed for next year	<b>6.75 %</b>	7.00 %	<b>4.00 %</b>	4.00 %
Rate to which the health care trend rate is assumed to decline (ultimate trend rate)	<b>4.50 %</b>	4.50 %	<b>N/A</b>	N/A
Year that the rate reaches the ultimate trend rate	<b>2029</b>	2026	<b>N/A</b>	N/A

Assumed health care cost trend rates have a significant effect on the amounts reported for the post-retirement benefit plan. A 1.0 percent change in assumed health care cost trend rates would have the following effects:

	1%	1%
	Increase	Decrease
Effect on the net periodic post-retirement health care benefit cost	\$ 677	\$ (530 )
Effect on the accumulated post-retirement benefit obligation	5,066	(4,107 )

**Benefit Obligation and Funded Status**

The following table provides a reconciliation of benefit obligations, plan assets and funded status of our plans:

Years Ended December 31,	Pension Benefits		Post-retirement Benefits	
	2018	2017	2018	2017
<i>Reconciliation of benefit obligation</i>				
Benefit obligation at beginning of year	<b>\$208,349</b>	\$171,876	<b>\$55,728</b>	\$46,785
Service cost	<b>8,701</b>	6,857	<b>2,998</b>	2,021
Interest cost	<b>7,500</b>	7,060	<b>2,009</b>	1,927
Actuarial loss	<b>(17,535 )</b>	26,963	<b>(12,094 )</b>	6,326
Adjustment for plan amendment	—	—	<b>(16,159 )</b>	—
Benefit payments	<b>(4,859 )</b>	(4,407 )	<b>(1,509 )</b>	(1,331 )
Benefit obligation at end of year <sup>(1)</sup>	<b>\$202,156</b>	\$208,349	<b>\$30,973</b>	\$55,728
<i>Reconciliation of fair value of plan assets</i>				
Fair value of plan assets at beginning of year	<b>\$157,644</b>	\$128,430	\$—	\$—
Actual return on plan assets	<b>(4,366 )</b>	22,225	—	—
Employer contributions	<b>16,400</b>	11,396	<b>1,509</b>	1,331
Benefit payments	<b>(4,859 )</b>	(4,407 )	<b>(1,509 )</b>	(1,331 )
Fair value of plan assets at end of year	<b>\$164,819</b>	\$157,644	\$—	\$—
Funded status at end of year	<b>\$(37,337 )</b>	\$(50,705 )	<b>\$(30,973 )</b>	\$(55,728 )

<sup>(1)</sup> For the pension plan, the benefit obligation is the projected benefit obligation. For the post-retirement benefit plan, the benefit obligation is the accumulated post-retirement benefit obligation.

Our accumulated pension benefit obligation was \$183,317 and \$184,436 at December 31, 2018 and 2017, respectively.

The following table displays the effect that the unrecognized prior service cost and unrecognized actuarial loss of our plans had on accumulated other comprehensive income ("AOCI"), as reported in the accompanying Consolidated Balance Sheets:

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Years Ended December 31	Pension Benefits		Post-retirement Benefits	
	2018	2017	2018	2017
<i>Amounts recognized in AOCI</i>				
Unrecognized prior service cost	\$—	\$—	\$(37,631)	\$(26,880)
Unrecognized actuarial (gain) loss	53,616	60,571	10,786	25,235
Total amounts recognized in AOCI	\$53,616	\$60,571	\$(26,845)	\$(1,645)

We anticipate amortization of the net actuarial losses for our pension plan in 2019 to be \$3,603. We anticipate amortization of the net actuarial losses for our post-retirement benefit plan in 2019 to be \$894.

**Net Periodic Benefit Cost**

The components of the net periodic benefit cost for our pension and post-retirement benefit plans are as follows:

Years Ended December 31,	Pension Plan			Post-retirement Benefit Plan		
	2018	2017	2016	2018	2017	2016
Net periodic benefit cost						
Service cost	\$8,701	\$6,857	\$6,490	\$2,998	\$2,021	\$3,728
Interest cost	7,500	7,060	6,654	2,009	1,927	3,015
Expected return on plan assets	(10,502)	(9,650)	(7,952)	—	—	—
Amortization of prior service cost	—	—	—	(5,409)	(5,409)	—
Amortization of net loss	4,287	3,562	3,968	2,355	1,846	1,518
Net periodic benefit cost	\$9,986	\$7,829	\$9,160	\$1,953	\$385	\$8,261

A portion of the service cost component of net periodic pension and postretirement benefit costs are capitalized and amortized as part of deferred acquisition costs and is included in the income statement line titled "amortization of deferred policy acquisition costs." The portion not related to the compensation and the other components of net periodic pension and postretirement benefit costs are included in the income statement line titled "other underwriting expenses."

**Projected Benefit Payments**

The following table summarizes the expected benefits to be paid from our plans over the next 10 years:

	2019	2020	2021	2022	2023	2024 - 2028
Pension benefits	\$6,280	\$6,870	\$7,570	\$8,230	\$8,940	\$55,930
Post-retirement benefits	\$960	\$1,030	\$1,120	\$1,210	\$1,300	\$8,480

**Profit-Sharing Plan**

We have a profit-sharing plan in which employees who meet service requirements are eligible to participate. The amount of our contribution is discretionary and is determined annually, but cannot exceed the amount deductible for federal income tax purposes. Our contribution to the profit-sharing plan for 2018, 2017 and 2016, was \$7,607, \$4,987 and \$2,904, respectively.

Table of Contents**NOTE 9. STOCK-BASED COMPENSATION****Non-Qualified Employee Stock Award Plan**

The United Fire Group, Inc. 2008 Stock Plan (the "2008 Stock Plan") authorized the issuance of restricted and unrestricted stock awards, stock appreciation rights, incentive stock options, and non-qualified stock options for up to 1,900,000 shares of United Fire common stock to employees. In May 2014, the Registrant's shareholders approved an additional 1,500,000 shares of United Fire common stock issuable at any time and from time to time pursuant to the 2008 Stock Plan, among other amendments, and renamed such plan as the United Fire Group, Inc. Stock Plan (as amended, the "Stock Plan"). At December 31, 2018, there were 890,857 authorized shares remaining available for future issuance. The Stock Plan is administered by the Board of Directors, which determines those employees who will receive awards, when awards will be granted, and the terms and conditions of the awards. The Board of Directors may also take any action it deems necessary and appropriate for the administration of the Stock Plan. Pursuant to the Stock Plan, the Board of Directors may, at its sole discretion, grant awards to our employees who are in positions of substantial responsibility with United Fire.

Options granted pursuant to the Stock Plan are granted to buy shares of United Fire's common stock at the market value of the stock on the date of grant. Options granted prior to March 2017 vest and are exercisable in installments of 20.0 percent of the number of shares covered by the option award each year from the grant date, unless the Board of Directors authorizes the acceleration of vesting. Options granted after March 2017 vest and are exercisable in installments of 33.3 percent of the number of shares covered by the option award each year from the grant date, unless the Board of Directors authorizes the acceleration of vesting. To the extent not exercised, vested option awards accumulate and are exercisable by the awardee, in whole or in part, in any subsequent year included in the option period, but not later than 10 years from the grant date. Restricted and unrestricted stock awards granted pursuant to the Stock Plan are granted at the market value of our common stock on the date of the grant. Restricted stock awards fully vest after 3 years or 5 years from the date of issuance, unless accelerated upon the approval of the Board of Directors, at which time United Fire common stock will be issued to the awardee. All awards are generally granted free of charge to the eligible employees of United Fire as designated by the Board of Directors.

The activity in the Stock Plan is displayed in the following table:

	<b>Year</b>	From
Authorized Shares Available for Future Award Grants	<b>Ended</b>	Inception to
	<b>December</b>	December
	<b>31, 2018</b>	31, 2018
Beginning balance	<b>996,828</b>	1,900,000
Additional shares authorized	—	1,500,000
Number of awards granted	<b>(151,096 )</b>	(3,023,067 )
Number of awards forfeited or expired	<b>45,125</b>	513,924
Ending balance	<b>890,857</b>	890,857
Number of option awards exercised	<b>238,719</b>	1,324,614
Number of unrestricted stock awards granted	<b>900</b>	9,370
Number of restricted stock awards vested	<b>20,025</b>	58,193

**Non-Qualified Non-Employee Director Stock Option and Restricted Stock Plan**

The United Fire Group, Inc. 2005 Non-Qualified Non-Employee Director Stock Option and Restricted Stock Plan (the "Director Plan") authorizes the issuance of restricted stock awards and non-qualified stock options to purchase shares of United Fire's common stock to non-employee directors. At December 31, 2018, we had 49,163 authorized shares available for future issuance.

The Board of Directors has the authority to determine which non-employee directors receive awards, when options and restricted stock shall be granted, the option price, the option expiration date, the date of grant, the vesting schedule of options or whether the options shall be immediately vested, the terms and conditions of options and restricted stock (other than those terms and conditions set forth in the plan) and the number of shares of common stock to be issued

pursuant to an option agreement or restricted stock agreement (subject to limits set forth in the

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plan). The Board of Directors may also take any action it deems necessary and appropriate for the administration of the Director Plan.

The activity in the Director Plan is displayed in the following table:

Authorized Shares Available for Future Award Grants	<b>Year Ended December 31, 2018</b>	From Inception to December 31, 2018
Beginning balance	<b>61,813</b>	300,000
Number of awards granted	<b>(12,650 )</b>	(274,840 )
Number of awards forfeited or expired	<b>—</b>	24,003
Ending balance	<b>49,163</b>	49,163
Number of option awards exercised	<b>28,680</b>	117,961
Number of restricted stock awards vested	<b>17,269</b>	71,541

**Stock-Based Compensation Expense**

In 2018, 2017 and 2016, we recognized stock-based compensation expense of \$5,249, \$4,808 and \$3,696, respectively. Stock-based compensation expense is recognized over the vesting period of the stock options.

As of December 31, 2018, we had \$6,803 in stock-based compensation expense that has yet to be recognized through our results of operations. We expect this compensation to be recognized in subsequent years according to the following table, except with respect to awards that are accelerated by the Board of Directors, in which case we will recognize any remaining compensation expense in the period in which the awards are accelerated.

2019	\$3,939
2020	2,289
2021	537
2022	38
2023	—
Total	\$6,803

**Analysis of Award Activity**

The analysis below details the option award activity for 2018 and the awards outstanding at December 31, 2018, for both of our plans and ad hoc options, which were granted prior to the adoption of the other plans:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Life ( <i>in years</i> )	Aggregate Intrinsic Value
Outstanding at January 1, 2018	1,101,051	\$ 31.16		
Granted	85,517	45.03		
Exercised	(267,399 )	28.30		
Forfeited	(20,266 )	35.27		
Expired	(1,000 )	34.39		
Outstanding at December 31, 2018	897,903	\$ 33.24	6.20	\$ 19,944
Exercisable at December 31, 2018	458,465	\$ 28.92	5.09	\$ 12,162

Intrinsic value is the difference between our share price on the last day of trading (i.e., December 31, 2018) and the price of the options when granted and represents the value that would have been received by option holders had they exercised their options on that date. These values change based on the fair market value of our shares. The intrinsic

value of options exercised totaled \$5,850, \$3,159 and \$4,339 in 2018, 2017 and 2016, respectively.



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The analysis below details the award activity for the restricted stock and restricted stock unit awards outstanding at December 31, 2018:

Restricted stock awards	Shares	Weighted-Average Grant Date Fair Value
Non-vested at January 1, 2018	267,799	\$ 36.66
Granted	79,739	46.02
Vested	(40,362 )	33.95
Forfeited	(23,201 )	33.86
Non-vested at December 31, 2018	283,975	\$ 39.90

In 2018, 2017 and 2016 we recognized \$3,877, \$2,987 and \$1,766, respectively, in compensation expense related to the restricted stock and restricted stock unit awards. At December 31, 2018, we had \$4,589 in compensation expense that has yet to be recognized through our results of operations related to the restricted stock and restricted stock unit awards. The intrinsic value of the non-vested restricted stock and restricted stock unit awards outstanding totaled \$15,746 and \$12,206 at December 31, 2018 and 2017, respectively.

**Assumptions**

The weighted-average grant-date fair value of the options granted under our plans has been estimated using the Black-Scholes option pricing model with the following weighted-average assumptions:

December 31,	2018	2017	2016
Risk-free interest rate	<b>2.79 %</b>	2.23 %	1.53 %
Expected volatility	<b>21.79 %</b>	27.58 %	25.44 %
Expected option life ( <i>in years</i> )	<b>7</b>	7	7
Expected dividends ( <i>in dollars</i> )	<b>\$1.12</b>	\$1.00	\$0.88
Weighted-average grant-date fair value of options granted during the year ( <i>in dollars</i> )	<b>\$8.90</b>	\$9.93	\$8.42

The following table summarizes information regarding the stock options outstanding and exercisable at December 31, 2018:

Range of Exercise Prices	Options Outstanding		Weighted-Average Exercise Price	Options Exercisable	
	Number Outstanding ( <i>in shares</i> )	Weighted-Average Remaining Contractual Life ( <i>in years</i> )		Number Exercisable ( <i>in shares</i> )	Weighted-Average Exercise Price
\$ 15.01 - 21.00	58,349	2.20	\$ 20.34	58,349	\$ 20.34
21.01 - 28.00	93,155	3.54	23.32	93,155	23.32
28.01 - 35.00	375,096	5.71	29.29	227,304	29.32
35.01 - 43.00	287,910	7.65	40.79	79,657	40.64
44.80 - 44.80	80,712	9.15	44.80	—	—
52.16 - 52.16	2,681	9.37	52.16	—	\$ —
\$ 15.01 - 52.16	897,903	6.20	\$ 33.24	458,465	\$ 28.92

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**NOTE 10. SEGMENT INFORMATION**

On September 19, 2017, the Company announced that it had agreed to sell its subsidiary, United Life, to Kuvare. The sale closed on March 30, 2018. As a result, our life insurance business was considered held for sale and reported as discontinued operations in the Consolidated Financial Statements and all comparable prior periods have been presented to conform to the current year presentation. For more information, refer to Note 17. "Discontinued Operations."

Prior to the announcement to sell United Life, we had two reportable business segments in our operations: property and casualty insurance and life insurance. The property and casualty insurance business has six domestic locations from which it conducts its business. The life insurance business operated from our home office. Because all of our insurance is sold domestically, we have no revenues allocable to foreign operations.

After the announcement of the sale of United Life, our continuing operations, the property and casualty insurance business, is reported as one reportable segment. The property and casualty insurance business profit or loss is consistent with consolidated reporting as disclosed on the Consolidated Statements of Income and Comprehensive Income. We analyze the property and casualty insurance business results based on profitability (i.e., loss ratios), expenses and return on equity. The Company's property and casualty insurance business was determined using a management approach to make decisions on operating matters, including allocating resources, assessing performance, determining which products to market and sell, determining distribution networks with insurance agents and monitoring the regulatory environment. The property and casualty insurance business products have similar economic characteristics and use a similar marketing and distribution strategy with our independent agents. The property and casualty insurance business geographic concentration did not change after the announcement of the sale of the life insurance business. We will continue to evaluate our continuing operations on the basis of both statutory accounting principles prescribed or permitted by our states of domicile and GAAP.

The accounting policies of our businesses are the same as those described in Note 1 to our Consolidated Financial Statements. We analyze results based on profitability (i.e., loss ratios), expenses and return on equity.

**Property and Casualty Insurance Business**

We write both commercial and personal lines of property and casualty insurance. We focus on our commercial lines, which represented 93.1% of our property and casualty insurance premiums earned for 2018. Our personal lines represented 6.9% of our property and casualty insurance premiums earned for 2018.

***Products***

Our primary commercial policies are tailored business packages that include the following coverages: fire and allied lines, other liability, automobile, workers' compensation and surety. Our personal lines consist primarily of automobile and fire and allied lines coverage, including homeowners.

***Pricing***

Pricing levels for our property and casualty insurance products are influenced by many factors, including an estimation of expected losses, the expenses of producing, issuing and servicing business and managing claims, the time value of money associated with such loss and expense cash flows, and a reasonable allowance for profit. We have a disciplined approach to underwriting and risk management that emphasizes profitable growth rather than premium volume or market share. Our insurance company subsidiaries are subject to state laws and regulations regarding rate and policy form approvals. The applicable state laws and regulations establish standards in certain lines of business to ensure that rates are not excessive, inadequate, unfairly discriminatory, or used to engage in unfair price competition. Our ability to increase rates and the relative timing of the process are dependent upon each respective state's requirements, as well as the competitive market environment.



Table of Contents**Seasonality**

Our property and casualty insurance business experiences some seasonality with regard to premiums written, which are generally highest in January and July and lowest during the fourth quarter. Although we experience some seasonality in our premiums written, premiums are earned ratably over the period of coverage. Losses and loss settlement expenses incurred tend to remain consistent throughout the year, with the exception of catastrophe losses which generally are highest in the second and third quarters. Catastrophes inherently are unpredictable and can occur at any time during the year from man-made or natural disaster events that include, but are not limited to, hail, tornadoes, hurricanes and windstorms.

**Premiums Earned**

The following table sets forth our net premiums earned:

Years Ended December 31,	2018	2017	2016
<b>Continuing Operations - Property and casualty insurance business</b>			
Net premiums earned			
Other liability	<b>\$311,931</b>	\$306,480	\$289,982
Fire and allied lines	<b>276,193</b>	270,716	265,221
Automobile	<b>313,521</b>	277,511	239,216
Workers' compensation	<b>95,203</b>	104,166	103,605
Fidelity and surety	<b>24,437</b>	24,981	22,507
Reinsurance assumed	<b>13,228</b>	10,650	12,765
Other	<b>2,938</b>	2,988	2,835
Total net premiums earned from continuing operations	<b>\$1,037,451</b>	\$997,492	\$936,131
<b>Discontinued Operations - Life insurance business</b>			
Net premiums earned			
Ordinary life (excluding universal life)	<b>\$7,068</b>	\$35,388	\$63,668
Universal life policy fees	<b>3,363</b>	13,145	11,577
Immediate annuities with life contingencies	<b>2,515</b>	11,691	10,533
Accident and health	<b>45</b>	1,096	1,434
Other	<b>12</b>	48	58
Total net premiums earned from discontinued operations	<b>\$13,003</b>	\$61,368	\$87,270

Total revenue includes sales to external customers and intercompany sales that are eliminated to arrive at the total revenues as reported in the accompanying Consolidated Statements of Income and Comprehensive Income. We account for intercompany sales on the same basis as sales to external customers.

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The following table sets forth our selected unaudited quarterly financial information from continuing operations:

(In Thousands Except Share Data)

Quarters	First	Second	Third	Fourth	Total
<b>Year Ended December 31, 2018</b>					
<b>Total revenues</b>	<b>\$250,795</b>	<b>\$275,399</b>	<b>\$291,910</b>	<b>\$252,062</b>	<b>\$1,070,166</b>
<b>Income (loss) before income taxes</b>	<b>21,573</b>	<b>(1,809 )</b>	<b>12,598</b>	<b>(41,512 )</b>	<b>(9,150 )</b>
<b>Net income (loss)</b>	<b>\$20,364</b>	<b>\$157</b>	<b>\$11,070</b>	<b>\$(29,336 )</b>	<b>\$2,255</b>
<b>Basic earnings per share <sup>(1)</sup></b>	<b>\$0.82</b>	<b>\$0.01</b>	<b>\$0.44</b>	<b>\$(1.17 )</b>	<b>\$0.09</b>
<b>Diluted earnings per share <sup>(1)</sup></b>	<b>0.80</b>	<b>0.01</b>	<b>0.43</b>	<b>(1.17 )</b>	<b>0.09</b>
Year Ended December 31, 2017					
Total revenues	\$251,278	\$258,487	\$269,617	\$273,355	\$1,052,737
Income (loss) before income taxes	23,006	(4,331 )	(32,394 )	29,369	15,650
Net income (loss)	\$18,584	\$109	\$(19,082 )	\$45,259	\$44,870
Basic earnings per share <sup>(1)</sup>	\$0.73	—	\$(0.77 )	\$1.81	\$1.79
Diluted earnings per share <sup>(1)</sup>	0.72	—	(0.77 )	1.78	1.75

(1) The sum of the quarterly reported amounts may not equal the full year, as each is computed independently.

The following table sets forth our selected unaudited quarterly financial information from discontinued operations:

(In Thousands Except Share Data)

Quarters	First	Second	Third	Fourth	Total
<b>Year Ended December 31, 2018</b>					
<b>Total revenues</b>	<b>\$24,755</b>	<b>\$—</b>	<b>\$—</b>	<b>\$—</b>	<b>\$24,755</b>
<b>Income (loss) before income taxes</b>	<b>(1,349 )</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>(1,349 )</b>
<b>Net income (loss)</b>	<b>\$(1,912 )</b>	<b>\$—</b>	<b>\$—</b>	<b>\$—</b>	<b>\$(1,912 )</b>
<b>Basic earnings per share <sup>(1)</sup></b>	<b>\$(0.08 )</b>	<b>\$—</b>	<b>\$—</b>	<b>\$—</b>	<b>\$(0.08 )</b>
<b>Diluted earnings per share <sup>(1)</sup></b>	<b>(0.07 )</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>(0.07 )</b>
Year Ended December 31, 2017					
Total revenues	\$31,781	\$28,492	\$27,054	\$28,386	\$115,713
Income before income taxes	2,083	4,386	1,880	2,294	10,643
Net income	\$1,352	\$2,849	\$1,218	\$734	\$6,153
Basic earnings per share <sup>(1)</sup>	\$0.05	\$0.11	\$0.05	\$0.03	\$0.24
Diluted earnings per share <sup>(1)</sup>	0.05	0.11	0.05	0.03	0.24

(1) The sum of the quarterly reported amounts may not equal the full year, as each is computed independently.

**NOTE 12. EARNINGS PER COMMON SHARE**

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings per share gives effect to all dilutive common shares outstanding during the reporting period. The dilutive shares we consider in our diluted earnings per share calculation relate to our outstanding stock options and restricted stock awards.

We determine the dilutive effect of our outstanding stock options using the "treasury stock" method. Under this method, we assume the exercise of all of the outstanding stock options whose exercise price is less than the weighted-average market value of our common stock during the reporting period. This method also assumes that the proceeds from the hypothetical stock option exercises are used to repurchase shares of our common stock at the weighted-average market value of the stock during the reporting period. The net of the assumed stock optio

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ns exercised and assumed common shares repurchased represents the number of dilutive common shares, which we add to the denominator of the earnings per share calculation.

The components of basic and diluted earnings per share were as follows:

	Years Ended December 31,					
	2018		2017		2016	
<i>(In Thousands Except Share and Per Share Data)</i>	Basic	Diluted	Basic	Diluted	Basic	Diluted
Net income from continuing operations	\$2,255	\$ 2,255	\$44,870	\$ 44,870	\$49,118	\$ 49,118
Weighted-average common shares outstanding	25,006,212	25,006,211	25,103,720	25,103,720	25,335,706	25,335,706
Add dilutive effect of restricted stock awards	—	273,544	—	250,530	—	155,059
Add dilutive effect of stock options	—	343,057	—	286,354	—	313,913
Weighted-average common shares	25,006,212	25,622,812	25,103,720	25,640,604	25,335,706	25,804,678
Earnings per common share from continuing operations	\$0.09	\$ 0.09	\$1.79	\$ 1.75	\$1.94	\$ 1.90
Earnings (loss) per common share from discontinued operations	(0.08 )	(0.07 )	0.24	0.24	0.03	0.03
Gain on sale of discontinued operations, net of taxes	\$1.10	\$ 1.07	\$—	\$—	\$—	\$—
Earnings per common share	\$1.11	\$ 1.08	\$2.03	\$ 1.99	\$1.97	\$ 1.93
Awards excluded from diluted calculation <sup>(1)</sup>	—	2,681	—	—	—	—

(1) Outstanding awards that are not "in-the-money" are excluded from the diluted earnings per share calculation because the effect of including them would have been anti-dilutive.

**NOTE 13. LEASE COMMITMENTS**

At December 31, 2018, we were obligated under noncancelable operating lease agreements for office space, vehicles, computer equipment and office equipment. Most of our leases include renewal options, purchase options or both. These provisions may be exercised by us upon the expiration of the related lease agreements. Rental expense under our operating lease agreements was \$6,644, \$7,197 and \$6,908 for 2018, 2017 and 2016, respectively. Our most significant lease commitment is for mainframe computer equipment. This lease was signed in November 2016 and has a term of 5 years. The monthly lease payments for this lease are \$154.

At December 31, 2018, our future minimum rental payments were as follows:

2019	\$7,214
2020	6,892
2021	4,635
2022	1,717
2023	1,043
Thereafter 181	
Total	\$21,682

**NOTE 14. CREDIT FACILITY**

On February 2, 2016, the Company, as borrower, entered into a Credit Agreement (the "Credit Agreement") by and among the Company, with the lenders from time to time party thereto and KeyBank National Association ("Key Bank"), as administrative agent, swingline lender and letter of credit issuer. The Credit Agreement provides for a \$50,000 four-year unsecured revolving credit facility that includes a \$20,000 letter of credit subfacility and a swingline subfacility in the amount up to \$5,000. The Credit Agreement allows the Company to increase the

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aggregate amount of the commitments thereunder by up to \$100,000, provided that no event of default has occurred and is continuing and certain other conditions are satisfied.

The Credit Agreement is available for the Company's general corporate purposes, including liquidity, acquisitions and working capital. All unpaid principal and accrued interest under the Credit Agreement is due and payable in full at maturity on February 2, 2020. Based on the type of loan, advances under the Credit Agreement would bear interest on either the London interbank offered rate ("LIBOR") or a base rate plus, in each case, a calculated margin amount.

The unused commitments under the Credit Agreement will be subject to a commitment fee that will be calculated at a per annum rate. The applicable margins for borrowings under the Credit Agreement and the commitment fee thereunder will be determined by reference to a pricing grid based on the Company's issuer credit rating by A.M. Best Company, Inc.

The Credit Agreement contains customary representations, conditions to borrowing, covenants and events of default, including certain covenants that limit or restrict, subject to certain exceptions, the ability of the Company and its subsidiaries to sell or transfer assets, enter into a merger or consolidate with another company, create liens, impose restrictions on subsidiary dividends, enter into sale-leaseback transactions, make investments or acquisitions, enter into certain reinsurance agreements, pay dividends during any period of default, enter into transactions with affiliates, change the nature of its business, or incur indebtedness. The Credit Agreement also includes financial covenants that require the Company to (i) maintain a minimum consolidated net worth, (ii) maintain a minimum consolidated statutory surplus and (iii) not exceed a 0.35 to 1.0 debt to total capitalization ratio. As of December 31, 2018 we were in compliance with all covenants of the Credit Agreement.

There was no outstanding balance on the Credit Agreement at December 31, 2018 or 2017. We did not incur any interest expense related to the Credit Agreement in 2018, 2017 or under our prior credit facility in 2016.

**NOTE 15. INTANGIBLE ASSETS**

The carrying value of our goodwill was \$15,091 at both December 31, 2018 and 2017, respectively. The goodwill is fully allocated to our property and casualty insurance business.

Our major classes of intangible assets are presented in the following table:

	Year Ended December 31,	
	2018	2017
Agency relationships	\$10,338	\$10,338
Accumulated amortization - agency relationships	(6,153 )	(5,566 )
	\$4,185	\$4,772
Software	\$3,260	\$3,260
Accumulated amortization - software	(3,260 )	(3,260 )
	\$—	\$—
Trade names	\$1,978	\$1,978
Accumulated amortization - trade names	(1,022 )	(890 )
	\$956	\$1,088
Favorable contract	\$286	\$286
Accumulated amortization - favorable contract	(286 )	(286 )
	\$—	\$—
State insurance licenses <sup>(1)</sup>	\$3,020	\$3,020
Net intangible assets	\$8,161	\$8,880

(1) The intangible asset for licenses has an indefinite life and therefore is not amortized.





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The estimated useful lives assigned to our major classes of amortizable intangible assets are as follows:

	Useful Life
Agency relationships	Fifteen years
Software	Two years
Trade names	Fifteen years
Favorable contract	Two years

Our estimated aggregate amortization expense for each of the next five years is as follows:

2019	\$ 709
2020	709
2021	709
2022	709
2023	709

**NOTE 16. ACCUMULATED OTHER COMPREHENSIVE INCOME**

The following table shows the changes in the components of our accumulated other comprehensive income (loss), net of tax, for the years ended December 31, 2018, 2017 and 2016:

	Net unrealized appreciation on investments	Liability for underfunded employee benefit costs	Total
Balance as of January 1, 2016	\$ 128,369	\$ (47,932 )	\$ 80,437
Change in accumulated other comprehensive income before reclassifications	8,461	19,529	27,990
Reclassification adjustments from accumulated other comprehensive income	(2,938 )	3,566	628
Balance as of December 31, 2016	\$ 133,892	\$ (24,837 )	\$ 109,055
Change in accumulated other comprehensive income before reclassifications	48,467	(19,878 )	28,589
Reclassification adjustments from accumulated other comprehensive income	(4,152 )	3,514	(638 )
Accumulated effect of change in enacted tax rate	36,658	(5,350 )	31,308
Balance as of December 31, 2017	\$ 214,865	\$ (46,551 )	\$ 168,314
Cumulative effect of change in accounting principle	<b>(191,244 )</b>		<b>(191,244 )</b>
Change in accumulated other comprehensive income before reclassifications	<b>(33,564 )</b>	<b>20,155</b>	<b>(13,409 )</b>
Reclassification adjustments from accumulated other comprehensive income	<b>620</b>	<b>5,247</b>	<b>5,867</b>
Balance as of December 31, 2018	<b>\$ (9,323 )</b>	<b>\$ (21,149 )</b>	<b>\$ (30,472 )</b>

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On September 18, 2017, we signed a definitive agreement to sell our subsidiary, United Life Insurance Company, to Kuvare for \$280,000 in cash, less a \$21 adjustment as set forth in the definitive agreement, for a net amount of \$279,979. The sale closed on March 30, 2018 and we reported an after-tax gain on the sale of discontinued operations of \$27,307. The life insurance business (previously reported as a separate segment) was considered held for sale and reported as discontinued operations and its financial position, results of operations and cash flows were reported separately for all periods presented, as applicable, unless otherwise noted.

UFG has agreed to provide services to Kuvare through a transition services agreement ("TSA"). The TSA ensures a seamless transfer of the business between UFG and Kuvare. The TSA includes, among other considerations, accounting management, human resources, legal and information technology services, from the closing date for up to 24 months. Since the close date, the Company has received \$414 as part of the TSA agreement.

The assets and liabilities associated with discontinued operations prior to the closing of the sale have been presented separately in our Consolidated Balance Sheets. The major assets and liability categories were as follows as of the dates indicated:

### Discontinued Operations Balance Sheets

	<b>December 31, 2017</b>
<i>(In Thousands, Except Share Data)</i>	
<b>Assets</b>	
Investments	
Fixed maturities	
Held-to-maturity, at amortized cost (fair value \$0 in 2018 and \$34 in 2017)	\$—34
Available-for-sale, at fair value (amortized cost \$0 in 2018 and \$1,412,291 in 2017)	—1,430,025
Equity Securities available-for-sale, at fair value (cost \$0 in 2018 and \$5,099 in 2017)	—23,653
Mortgage loans	—3,435
Policy loans	—5,815
Other long-term investments	—16,437
	—1,479,399
Cash and cash equivalents	—15,851
Deferred policy acquisition costs	—71,151
Other assets	—19,733
<b>Total assets held for sale</b>	<b>\$—1,586,134</b>
<b>Liabilities</b>	
Future policy benefits and losses	\$—1,320,401
Deferred income taxes	—18,716
Accrued expenses and other liabilities	—8,018
<b>Total liabilities held for sale</b>	<b>\$—1,347,135</b>

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Summary operating results of discontinued operations were as follows for the periods indicated:

## Discontinued Operations Statements of Income

	For the Years Ended		
	December 31,		
(In Thousands, Except Share Data)	2018	2017	2016
<b>Revenues</b>			
Net premiums earned	\$13,003	\$61,368	\$87,270
Investment income, net of investment expenses	12,663	49,720	51,538
Total net realized investment gains (losses)	(1,057 )	4,008	1,156
Other income	146	617	621
<b>Total revenues</b>	<b>\$24,755</b>	<b>\$115,713</b>	<b>\$140,585</b>
<b>Benefits, Losses and Expenses</b>			
Losses and loss settlement expenses	\$10,823	\$40,451	\$31,365
Increase in liability for future policy benefits	5,023	27,632	59,969
Amortization of deferred policy acquisition costs	1,895	5,181	8,121
Other underwriting expenses	3,864	13,281	19,881
Interest on policyholders' accounts	4,499	18,525	20,079
<b>Total benefits, losses and expenses</b>	<b>\$26,104</b>	<b>\$105,070</b>	<b>\$139,415</b>
Income (loss) from discontinued operations before income taxes	\$(1,349 )	\$10,643	\$1,170
Federal income tax expense	563	4,490	384
<b>Net income (loss) from discontinued operations</b>	<b>\$(1,912 )</b>	<b>\$6,153</b>	<b>\$786</b>
<b>Earnings per common share from discontinued operations:</b>			
<b>Basic</b>	<b>\$(0.08 )</b>	<b>\$0.24</b>	<b>\$0.03</b>
<b>Diluted</b>	<b>(0.07 )</b>	<b>0.24</b>	<b>0.03</b>

The Company's Consolidated Statement of Cash Flows presents operating, investing and financing cash flows of the discontinued operations separately. The Company's cash management and financial management of both continued and discontinued operations is consolidated as a centralized corporate function in our Finance Department.

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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Shareholders  
United Fire Group, Inc.

**Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of United Fire Group, Inc. (the Company) as of December 31, 2018 and 2017, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and financial statement schedules listed in the Index at Item 15(a)(2) (collectively referred to as the “financial statements”). In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company at December 31, 2018 and 2017, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework), and our report dated February 28, 2019 expressed an unqualified opinion thereon.

**Adoption of ASU No. 2016-01**

As discussed in Note 1 to the financial statements, the Company changed its method of accounting for the change in the fair value of equity securities in the 2018 financial statements on a prospective basis due to the adoption of ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*.

**Basis for Opinion**

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/  
Ernst  
&  
Young  
LLP

Ernst  
&  
Young  
LLP

We have served as the Company's auditor since 2002.

Des Moines, Iowa  
February 28, 2019

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**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

**EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures, as of the end of the period covered by this report, were designed and functioning effectively to provide reasonable assurance that the information required to be disclosed by us in reports filed or submitted under the Exchange Act are recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. We believe that a control system, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the control system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

**MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

The management of United Fire Group, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. United Fire Group, Inc.'s internal control over financial reporting is a process designed under the supervision of its Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of its Consolidated Financial Statements for external purposes in accordance with U.S. generally accepted accounting principles.

As of December 31, 2018, United Fire Group, Inc.'s management assessed the effectiveness of United Fire Group Inc.'s internal control over financial reporting based on the criteria for effective internal control over financial reporting established in "Internal Control — Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework). Based on the assessment, United Fire Group, Inc.'s management determined that effective internal control over financial reporting was maintained as of December 31, 2018, based on those criteria.

Ernst & Young LLP, the independent registered public accounting firm that audited the Consolidated Financial Statements of United Fire Group, Inc. included in this Annual Report on Form 10-K, has audited the effectiveness of internal control over financial reporting as of December 31, 2018. Their attestation report, which expresses an unqualified opinion on the effectiveness of United Fire Group, Inc.'s internal control over financial reporting as of December 31, 2018, is included in this Item under the heading "Report of Independent Registered Public Accounting Firm."

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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Shareholders  
United Fire Group, Inc.

**Opinion on Internal Control over Financial Reporting**

We have audited United Fire Group, Inc.'s (the Company) internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of United Fire Group, Inc. as of December 31, 2018 and 2017, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018 of the Company and our report dated February 28, 2019 expressed an unqualified opinion thereon.

**Basis for Opinion**

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Annual Report. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

**Definition and Limitations of Internal Control Over Financial Reporting**

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.





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Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP  
Ernst & Young LLP

Des Moines, Iowa  
February 28, 2019

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**CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

There have been no changes in our internal control over financial reporting (as defined in Exchange Act Rules 13a-15 and 15d-15) that occurred during the fiscal quarter ended December 31, 2018, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**ITEM 9B. OTHER INFORMATION**

None.

**PART III.**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by Item 10 regarding the Company's executive officers is included in "Executive Officers of the Company" under Part I, Item 1 of this report.

The information required by this Item regarding our directors and corporate governance matters is included under the captions "Board of Directors," subheading "Corporate Governance" and "Proposal One-Election of Directors," in our definitive proxy statement for our annual meeting of shareholders to be held on May 15, 2019 (the "2019 Proxy Statement") and is incorporated herein by reference.

The information regarding our Code of Ethics is included under the caption "Board of Directors," subheading "Corporate Governance," subpart "Code of Ethics" in our 2019 Proxy Statement and is incorporated herein by reference.

The information required by this Item regarding compliance with Section 16(a) of the Exchange Act is included under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in our 2019 Proxy Statement and is incorporated herein by reference.

**ITEM 11. EXECUTIVE COMPENSATION**

The information required under this Item regarding our executive compensation and our Compensation Committee Report is included under the caption "Executive Compensation" in our 2019 Proxy Statement and is incorporated herein by reference. The information required by this Item regarding Compensation Committee interlocks and insider participation is included under the caption "Board of Directors," subheading "Committees of the Board," subheading "Compensation Committee," subpart "Compensation Committee Interlocks and Insider Participation" in our 2019 Proxy Statement and is incorporated herein by reference.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS**

The information required under this Item is included under the captions "Security Ownership of Certain Beneficial Owners," "Security Ownership of Management" and "Securities Authorized for Issuance under Equity Compensation Plans" in our 2019 Proxy Statement and is incorporated herein by reference.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required under this Item is included under the captions "Board of Directors" and "Transactions with Related Persons" in our 2019 Proxy Statement and is incorporated herein by reference.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required under this Item is included under the caption "Proposal Two - Ratification of the Audit Committee's Appointment of Independent Registered Public Accounting Firm," subheading "Information About Our Independent Registered Public Accounting Firm" in our 2019 Proxy Statement and is incorporated herein by reference.

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**PART IV.**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

We have filed the following documents as part of this Annual Report on Form 10-K:

	Page
<u>(a) 1. Financial Statements</u>	
<u>Consolidated Balance Sheets at December 31, 2018 and 2017</u>	<u>66</u>
<u>Consolidated Statements of Income and Comprehensive Income for the three years ended December 31, 2018</u>	<u>67</u>
<u>Consolidated Statements of Stockholders' Equity for the three years ended December 31, 2018</u>	<u>68</u>
<u>Consolidated Statements of Cash Flows for the three years ended December 31, 2018</u>	<u>69</u>
<u>Notes to Consolidated Financial Statements</u>	<u>71</u>
<u>(a) 2. Financial Statement Schedules required to be filed by Item 8 of this Form:</u>	
<u>Schedule I. Summary of Investments — Other than Investments in Related Parties</u>	<u>147</u>
<u>Schedule II. Condensed Financial Statements of Parent Company</u>	<u>148</u>
<u>Schedule III: Supplementary Insurance Information</u>	<u>151</u>
<u>Schedule IV: Reinsurance</u>	<u>152</u>
<u>Schedule V: Valuation and Qualifying Accounts</u>	<u>153</u>
<u>Schedule VI: Supplemental Information Concerning Property and Casualty Insurance Operations</u>	<u>154</u>
All other schedules have been omitted as not required, not applicable, not deemed material or because the information is included in the Consolidated Financial Statements.	

Table of Contents(a) 3. Exhibit Index:

Exhibit number	Exhibit description	Filed herewith	Incorporated by reference			Filing date
			Form	Period ended	Exhibit	
2.1†	<u>Stock Purchase Agreement, dated as of September 18, 2017, between United Fire &amp; Casualty Company and Kuvare US Holdings, Inc., including the exhibits attached thereto (incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K, Filed on September 19, 2017).</u>		8-K		2.1	9/19/2017
3.1	<u>Articles of Incorporation of United Fire Group, Inc.</u>		S-4		Annex II	5/25/2011
3.2	<u>Articles of Amendment to Articles of Incorporation of United Fire Group, Inc.</u>		8-K/A		3.1	5/26/2015
3.3	<u>Bylaws of United Fire Group, Inc.</u>		S-4		Annex III	5/25/2011
10.1 *	<u>United Fire &amp; Casualty Company Employee Stock Purchase Plan, Amended and Restated as of November 16, 2017</u>		10-K	12/31/2007	10.2	2/27/2008
10.2 *	<u>United Fire &amp; Casualty Company 2005 Non-Qualified Non-Employee Director Stock Option and Restricted Stock Plan (as amended)</u>		DEF14A		Exhibit A	4/18/2011
10.4 *	<u>United Fire Group, Inc. Amended and Restated Annual Incentive Plan</u>		10-K	12/31/2011	10.4	3/15/2012
10.5 *	<u>United Fire &amp; Casualty Company Non-qualified Deferred Compensation Plan</u>		10-Q	9/30/2007	10.3	10/25/2007
10.6 *	<u>United Fire Group, Inc. Stock Plan, amended as of February 21, 2014 (amending and restating the United Fire &amp; Casualty Company 2008 Stock Plan) (the "Stock Plan")</u>		DEF14A		App A	4/8/2014
10.7 *	<u>Form of Non-qualified Stock Option Agreement pursuant to the United Fire &amp; Casualty Company, Inc. Nonqualified Employee Stock Option Plan</u>		10-K	12/31/2007	10.7	2/27/2008
10.8 *	<u>Form of Stock Option Issued Pursuant to the 2005 Non-Qualified Non-Employee Director Stock Option and Restricted Stock Plan</u>		10-K	12/31/2007	10.8	2/27/2008
10.9 *	<u>Form of Stock Award Agreement Under the Stock Plan</u>		8-K		99.2	5/22/2008
10.10 *	<u>Form of Non-Qualified Stock Option Agreement for the Purchase of Stock under the Stock Plan</u>		8-K		99.3	5/22/2008
10.11 *	<u>Form of Incentive Stock Option Agreement for the Purchase of Stock under the Stock Plan</u>		8-K		99.4	5/22/2008
10.12 *	<u>Amendment to Non-qualified Stock Option Agreements for John A. Rife pursuant to the Stock Plan</u>		8-K/A		99.1	2/24/2009
10.13 *	<u>Form of United Fire Group, Inc. Restricted Stock Agreement Under the 2005 Non-Qualified Non-Employee Director Stock Option Plan</u>		10-K	12/31/2011	10.14	3/15/2012
10.14 *	<u>Form of United Fire Group, Inc. Restricted Stock Agreement Under the 2005 Non-Qualified Non-Employee Director Stock Option Plan</u>		10-Q	6/30/2016	10.1	8/3/2016
10.14 *	<u>United Fire Group, Inc. Plan for Allocation of Equity Compensation to Management Team</u>		10-K	12/31/2011	10.15	3/15/2012
10.15 *	<u>Deferred Compensation Plan for United Fire Group, Inc. Non-Employee Directors</u>		8-K		10.1	11/19/2012

\*Indicates a management contract or compensatory plan or arrangement.

† The schedules to this Exhibit have been omitted in accordance with Regulation S-K Item 601(b)(2). The registrant agrees to furnish a copy of all omitted schedules to the Securities and Exchange Commission upon its request.

Table of Contents(a) 3. Exhibit Index (continued):

Exhibit number	Exhibit description	Filed herewith	Incorporated by reference		
			Form	Period ended	Exhibit Filing date
10.16*	<u>Executive Nonqualified Excess Plan</u>		8-K		10.1 5/22/2014
10.17*	<u>Executive Nonqualified "Excess Plan" Adoption Agreement</u>		8-K		10.2 5/22/2014
10.18*	<u>United Fire &amp; Casualty Company Rabbi Directed Trust Agreement</u>		8-K		10.3 5/22/2014
10.19*	<u>Form of United Fire Group, Inc. Change in Control Severance Agreement</u>		8-K		10.4 5/22/2014
10.20*	<u>Amendment Number One to United Fire &amp; Casualty Company Nonqualified Deferred Compensation Plan</u>		8-K		10.5 5/22/2014
10.21*	<u>Form of Non-Qualified Employee Stock Option Agreement for Purchase of Stock Under the United Fire Group, Inc. 2008 Stock Plan</u>		10-Q	6/30/14	10.7 8/5/2014
10.22*	<u>Form of Stock Award Agreement under the United Fire Group, Inc. Stock Plan</u>		10-Q	6/30/14	10.8 8/5/2014
10.23*	<u>Form of Stock Award Agreement ( Restricted Stock Units-Performance Units) Under the Stock Plan</u>		10-Q	3/31/17	10.1 5/3/2017
10.24	<u>Credit Agreement dated as of February 2, 2016, by and among United Fire Group, Inc., as borrower, the lenders from time to time party thereto, and KeyBank National Association, as administrative agent, swingline lender and letter of credit issuer.</u>		8-K		10.1 2/5/2016
21	<u>Subsidiaries of the Registrant</u>	X			
23.1	<u>Consent of Ernst &amp; Young LLP, Independent Registered Public Accounting Firm</u>	X			
23.2	<u>Consent of Griffith, Ballard &amp; Company, Independent Actuary</u>	X			
23.3	<u>Consent of Regnier Consulting Group, Inc., Independent Actuary</u>	X			

\*Indicates a management contract or compensatory plan or arrangement.

Table of Contents(a) 3. Exhibit Index (continued):

Exhibit number	Exhibit description	Filed herewith	Incorporated by reference		
			Form	Period ending	Exhibit Filing date
31.1	<u>Certification of Randy A. Ramlo Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>	X			
31.2	<u>Certification of Dawn M. Jaffray Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>	X			
32.1	<u>Certification of Randy A. Ramlo Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>	X			
32.2	<u>Certification of Dawn M. Jaffray Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>	X			
101.1	<u>The following financial information from United Fire Group, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2018 formatted in XBRL: (i) Consolidated Balance Sheets at December 31, 2018 and 2017; (ii) Consolidated Statements of Income and Comprehensive Income for the years ended December 31, 2018, 2017 and 2016; (iii) Consolidated Statement of Stockholders' Equity for the years ended December 31, 2018, 2017 and 2016; (iv) Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017 and 2016; and (v) Notes to Consolidated Financial Statements.</u>	X			

Table of Contents**Schedule I. Summary of Investments — Other than Investments in Related Parties**

December 31, 2018

*(In thousands)*

Type of Investment	Cost or Amortized Cost	Fair Value	Amounts at Which Shown in Balance Sheet
Fixed maturities			
Bonds			
United States Government and government agencies and authorities	\$243,167	\$242,100	\$242,100
States, municipalities and political subdivisions	939,068	936,060	936,060
Foreign governments	9,698	9,716	9,716
Public utilities	56,808	56,059	56,059
All other bonds	520,803	516,044	516,044
Redeemable preferred stock	3,022	2,749	2,749
Total fixed maturities	\$1,772,566	\$1,762,728	\$1,762,728
Equity securities			
Common stocks			
Public utilities	\$4,226	\$15,949	\$15,949
Banks, trusts and insurance companies	13,737	101,555	101,555
Industrial, miscellaneous and all other	41,430	125,206	125,206
Nonredeemable preferred stocks	5,426	5,651	5,651
Total equity securities	\$64,819	\$248,361	\$248,361
Mortgage loans on real estate	\$25,828	\$26,021	\$25,782
Other long-term investments	37,077	37,077	37,077
Short-term investments	175	175	175
Total investments	\$1,900,465	\$2,074,362	\$2,074,123





Table of Contents**Schedule II. Condensed Financial Statements of Parent Company**

## United Fire Group, Inc. (parent company only)

## Condensed Balance Sheets

	December 31,	
	<b>2018</b>	2017
<i>(In thousands, except share data)</i>		
<b>Assets</b>		
Fixed maturities		
Held-to-maturity, at amortized cost (fair value \$0 in 2018 and \$150 in 2017)	\$—	\$150
Available-for-sale, at fair value (amortized cost \$150 in 2018 and \$0 in 2017)	<b>150</b>	—
Investment in subsidiary	<b>877,893</b>	967,590
Cash and cash equivalents	<b>9,186</b>	4,537
Federal income tax receivable	<b>1,165</b>	1,095
Accrued investment income	<b>1</b>	1
<b>Total assets</b>	<b>\$888,395</b>	\$973,373
<b>Liabilities and stockholders' equity</b>		
<b>Liabilities</b>		
	<b>\$20</b>	\$—
<b>Stockholders' equity</b>		
Common stock, \$0.001 par value, authorized 75,000,000 shares; 25,097,408 and 24,916,806 issued and outstanding in 2018 and 2017, respectively	<b>\$25</b>	\$25
Additional paid-in capital	<b>203,350</b>	196,334
Retained earnings	<b>715,472</b>	608,700
Accumulated other comprehensive income, net of tax	<b>(30,472)</b>	168,314
<b>Total stockholders' equity</b>	<b>\$888,375</b>	\$973,373
<b>Total liabilities and stockholders' equity</b>	<b>\$888,395</b>	\$973,373

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8 of this Annual Report on Form 10-K.



Table of Contents**Schedule II. Condensed Financial Statements of Parent Company (continued)**United Fire Group, Inc. (parent company only)  
Condensed Statements of Income and Comprehensive Income

<i>(In thousands)</i>	For the Years Ended December 31,		
	<b>2018</b>	2017	2016
<b>Revenues</b>			
Investment income	<b>\$396</b>	\$133	\$66
<b>Total revenues</b>	<b>396</b>	133	66
<b>Expenses</b>			
Other operating expenses	<b>\$95</b>	\$103	\$73
<b>Total expenses</b>	<b>95</b>	103	73
<b>Income (loss) before income taxes and equity in net income of subsidiary</b>	<b>301</b>	30	(7 )
Federal income tax benefit	<b>(1,165)</b>	(1,060)	(3 )
<b>Net income (loss) before equity in net income of subsidiary</b>	<b>\$1,466</b>	\$1,090	\$(4 )
<b>Equity in net income of subsidiary</b>	<b>26,184</b>	49,933	49,908
<b>Net income</b>	<b>\$27,650</b>	\$51,023	\$49,904
<b>Other comprehensive income (loss)</b>			
Change in unrealized appreciation on investments held by subsidiary	<b>\$(50,985)</b>	\$72,251	\$13,017
Change in liability for underfunded employee benefit plans of subsidiary	<b>25,513</b>	(26,122)	)30,045
Other comprehensive income (loss), before tax and reclassification adjustments	<b>\$(25,472)</b>	\$46,129	\$43,062
Income tax effect	<b>5,349</b>	(17,540)	(15,072 )
Other comprehensive income (loss), after tax, before reclassification adjustments	<b>\$(20,123)</b>	\$28,589	\$27,990
Reclassification adjustment for net realized gains of the subsidiary included in income	<b>784</b>	(6,390)	(4,520 )
Reclassification adjustment for employee benefit costs of the subsidiary included in expense	<b>6,642</b>	5,408	5,486
Total reclassification adjustments, before tax	<b>\$7,426</b>	\$(982)	)\$966
Income tax effect	<b>(1,559)</b>	)344	(338 )
Total reclassification adjustments, after tax	<b>\$5,867</b>	\$(638)	)\$628
<b>Comprehensive income</b>	<b>\$13,394</b>	\$78,974	\$78,522

United Fire Group, Inc. and its subsidiaries file a consolidated federal income tax return. The federal income tax provision represents an allocation under its tax allocation agreements.

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8 of this Annual Report on Form 10-K.



Table of Contents**Schedule II. Condensed Financial Statements of Parent Company (continued)**United Fire Group, Inc. (parent company only)  
Condensed Statements of Cash Flows

<i>(In thousands)</i>	For the Years Ended December		
	31, <b>2018</b>	2017	2016
<b>Cash flows from operating activities</b>			
Net income	<b>\$27,650</b>	\$51,023	\$49,904
Adjustments to reconcile net income to net cash provided by operating activities			
Equity in net income of subsidiary	<b>(26,184)</b>	(49,933)	(49,908)
Dividends received from subsidiary	<b>105,000</b>	40,000	24,000
Other, net	<b>1,824</b>	1,415	2,995
Total adjustments	<b>\$80,640</b>	\$(8,518)	\$(22,913)
Net cash provided by operating activities	<b>\$108,290</b>	\$42,505	\$26,991
<b>Cash flows from investing activities</b>			
Proceeds from maturity of held-to-maturity investments	\$—	\$150	\$—
Purchase of held-to-maturity investments	—	(150)	—
Net cash used in investing activities	\$—	\$—	\$—
<b>Cash flows from financing activities</b>			
Payment of cash dividends	<b>\$(105,408)</b>	\$(27,337)	\$(24,591)
Repurchase of common stock	<b>(5,404)</b>	(29,784)	(3,746)
Issuance of common stock	<b>7,171</b>	4,828	9,922
Tax impact from issuance of common stock	—	—	(816)
Net cash used in financing activities	<b>\$(103,641)</b>	\$(52,293)	\$(19,231)
Net change in cash and cash equivalents	<b>\$4,649</b>	\$(9,788)	\$7,760
Cash and cash equivalents at beginning of period	<b>4,537</b>	14,325	6,565
<b>Cash and cash equivalents at end of year</b>	<b>\$9,186</b>	\$4,537	\$14,325

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8 of this Form 10-K.

Table of Contents**Schedule III. Supplementary Insurance Information**

<i>(In thousands)</i>	Deferred Policy Acquisition Costs	Future Policy Benefits, Losses, Claims and Loss Expenses	Unearned Premiums	Earned Premium Revenue	Investment Income, Net	Benefits, Claims, Losses and Settlement Expenses	Amortization of Deferred Policy Acquisition Costs	Other Underwriting Expenses	Interest on Policyholders' Accounts	Premiums Written <sup>(2)</sup>
Year Ended December 31, 2018										
<b>Continuing Operations</b>	\$ 92,796	\$ 1,312,483	\$ 492,918	\$ 1,037,451	\$ 52,894	\$ 731,611	\$ 206,232	\$ 141,473	\$ —	\$ 1,061,664
<b>Discontinued Operations<sup>(1)</sup></b>	—	—	—	13,003	12,663	15,846	1,895	3,864	4,499	—
<b>Total</b>	\$ 92,796	\$ 1,312,483	\$ 492,918	\$ 1,050,454	\$ 65,557	\$ 747,457	\$ 208,127	\$ 145,337	\$ 4,499	\$ 1,061,664
Year Ended December 31, 2017										
Continuing Operations	\$ 88,102	\$ 1,224,183	\$ 465,391	\$ 997,492	\$ 51,190	\$ 725,713	\$ 207,746	\$ 103,628	\$ —	\$ 1,019,113
Discontinued Operations <sup>(1)</sup>	71,151	1,320,401	67	61,368	49,720	68,083	5,181	13,281	18,525	—
<b>Total</b>	\$ 159,253	\$ 2,544,584	\$ 465,458	\$ 1,058,860	\$ 100,910	\$ 793,796	\$ 212,927	\$ 116,909	\$ 18,525	\$ 1,019,113
Year Ended December 31, 2016										
Continuing Operations	\$ 93,362	\$ 1,123,896	\$ 443,802	\$ 936,131	\$ 55,284	\$ 652,433	\$ 202,892	\$ 83,540	\$ —	\$ 964,970
Discontinued Operations <sup>(1)</sup>	70,750	1,350,503	71	87,270	51,538	91,334	8,121	19,881	20,079	—
<b>Total</b>	\$ 164,112	\$ 2,474,399	\$ 443,873	\$ 1,023,401	\$ 106,822	\$ 743,767	\$ 211,013	\$ 103,421	\$ 20,079	\$ 964,970

(1) Annuity deposits are included in future policy benefits, losses, claims and loss expenses.

(2) Pursuant to Regulation S-X, premiums written does not apply to life insurance companies.

Table of Contents**Schedule IV. Reinsurance**

<i>(In thousands)</i>	Gross Amount	Ceded to Other Companies	Assumed From Other Companies	Net Amount	Percentage of Amount Assumed to Net Earned
<b>Year Ended December 31, 2018</b>					
<b>Life insurance in force</b>	\$—	\$—	\$ —	\$—	
<b>Premiums earned</b>					
<b>Continuing Operations - Property and casualty insurance</b>	<b>\$1,083,981</b>	<b>\$63,487</b>	<b>\$ 16,957</b>	<b>\$1,037,451</b>	<b>1.63 %</b>
<b>Discontinued Operations - Life, accident and health insurance</b>	—	—	—	—	— %
<b>Total</b>	<b>\$1,083,981</b>	<b>\$63,487</b>	<b>\$ 16,957</b>	<b>\$1,037,451</b>	<b>1.63 %</b>
<b>Year Ended December 31, 2017</b>					
Life insurance in force	\$5,309,508	\$1,014,794	\$ —	\$4,294,714	
Premiums earned					
Continuing Operations - Property and casualty insurance	\$1,043,738	\$61,305	\$ 15,059	\$997,492	1.51 %
Discontinued Operations - Life, accident and health insurance	64,090	2,722	—	61,368	— %
Total	\$1,107,828	\$64,027	\$ 15,059	\$1,058,860	1.42 %
<b>Year Ended December 31, 2016</b>					
Life insurance in force	\$5,314,548	\$1,023,197	\$ —	\$4,291,351	
Premiums earned					
Continuing Operations - Property and casualty insurance	\$977,090	\$57,996	\$ 17,037	\$936,131	1.82 %
Discontinued Operations - Life, accident and health insurance	90,038	2,768	—	87,270	— %
Total	\$1,067,128	\$60,764	\$ 17,037	\$1,023,401	1.66 %



Table of Contents**Schedule V. Valuation And Qualifying Accounts***(In thousands)*

Description	Balance at beginning of period	Charged to costs and expenses	Deductions	Balance at end of period
Allowance for bad debts				
<b>Year Ended December 31, 2018</b>	<b>\$ 1,255</b>	<b>\$ —</b>	<b>—\$ 470</b>	<b>\$ 785</b>
Year Ended December 31, 2017	1,255	—	—	1,255
Year Ended December 31, 2016	867	388	—	1,255
Deferred tax asset valuation allowance <sup>(1)</sup>				
<b>Year Ended December 31, 2018</b>	<b>\$ 329</b>	<b>\$ —</b>	<b>—\$ 329</b>	<b>\$ —</b>
Year Ended December 31, 2017	718	—	389	329
Year Ended December 31, 2016	1,265	—	547	718

(1) Recorded in connection with the purchase of American Indemnity Financial Corporation in 1999.

Table of Contents**Schedule VI. Supplemental Information Concerning Property and Casualty Insurance Operations***(In thousands)*

Affiliation with Registrant: United Fire & Casualty Company and consolidated property and casualty subsidiaries	Deferred Policy Acquisition Costs	Reserves for Unpaid Claims and Claim Adjustment Expenses	Unearned Premiums	Earned Premiums	Net Realized Investment Gains	Net Investment Income	Claims and Claim Adjustment Expenses Incurred Related to:		Amortization of Deferred Policy Acquisition Costs <sup>(1)</sup>	Paid Claims and Claim Adjustment Expenses	Premiums Written
							Current Year	Prior Years			
2018	\$ 92,796	\$ 1,312,483	\$ 492,918	\$ 1,037,451	\$ (20,179 )	\$ 52,894	\$ 785,778	\$ (54,167 )	\$ 206,232	\$ 640,534	\$ 1,061,664
2017	\$ 88,102	\$ 1,224,183	\$ 465,391	\$ 997,492	\$ 4,055	\$ 51,190	\$ 779,966	\$ (54,253 )	\$ 207,746	\$ 625,503	\$ 1,019,113
2016	\$ 93,362	\$ 1,123,896	\$ 443,802	\$ 936,131	\$ 4,947	\$ 55,284	\$ 683,662	\$ (31,229 )	\$ 202,892	\$ 537,573	\$ 964,970

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**ITEM 16. FORM 10-K SUMMARY**

None.

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**UNITED FIRE GROUP, INC.**

By: /s/ Randy A. Ramlo

Randy A. Ramlo, Chief Executive Officer, Director and Principal Executive Officer

Date: 2/28/2019

By: /s/ Dawn M. Jaffray

Dawn M. Jaffray, Senior Vice President, Chief Financial Officer, Principal Financial Officer and Principal Accounting Officer

Date: 2/28/2019

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By /s/ Jack B. Evans

Jack B. Evans, Chairman and Director

Date 2/28/2019

By /s/ John Paul E.

Besong  
John Paul E. Besong,  
Director

Date 2/28/2019

By /s/ Scott L. Carlton

Scott L. Carlton, Director

Date 2/28/2019

By: /s/ Brenda K. Clancy

Brenda K. Clancy,  
Director

Date 2/28/2019

By /s/ Christopher R. Drahozal

Christopher R. Drahozal, Director

Date 2/28/2019

By /s/ Sarah Fisher

Gardial  
Sarah Fisher Gardial,  
Director

Date 2/28/2019

By /s/ Dawn M. Jaffray

Dawn M. Jaffray, Senior Vice President, Chief Financial Officer, Principal Financial Officer and Principal Accounting Officer

Date 2/28/2019

By /s/ George D. Milligan

George D. Milligan,  
Director

Date 2/28/2019

By /s/ James W. Noyce

James W. Noyce, Vice Chairman and Director

Date 2/28/2019

By /s/ Mary K. Quass

Mary K. Quass,  
Director

Date 2/28/2019

By /s/ Randy A. Ramlo

Randy A. Ramlo, Chief Executive Officer, Director and Principal Executive Officer

Date 2/28/2019

By /s/ Kyle D. Skogman

Kyle D. Skogman,  
Director

Date 2/28/2019

By /s/ Susan E. Voss

Susan E. Voss, Director  
Date 2/28/2019

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