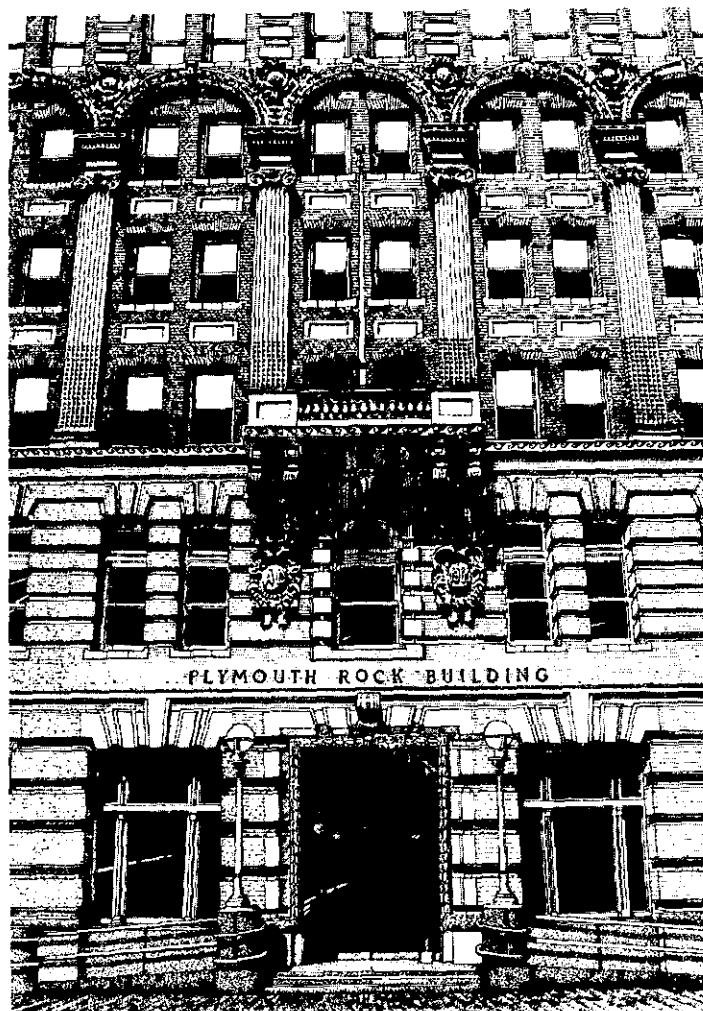


# The Plymouth Rock Company



## 1994 Annual Report

**The Plymouth Rock Company**  
695 Atlantic Avenue  
Boston, Massachusetts 02111

**Chairman's Letter**

February 24, 1995

To Our Shareholders:

Three adverse developments, and one favorable trend, colored the year just ended. Last year's report to shareholders warned that we were nearing the peak of a cycle in the profitability of Massachusetts auto insurance. I must now report that we are past the peak. Although the 1994 results were unaffected by this change, future performance inevitably will be. Of more immediate impact in 1994 were a record harsh winter and bond market conditions that made the winter look mild. The good news, meanwhile, is that our course has been further established with respect to diversification. We are expanding our personal lines involvement in other states and growing our service businesses. Happy with the direction of these advances, and planning to step up the pace in the coming year, I am on balance optimistic. The cyclical determinants of our prosperity may be weaker for a time, but the permanent foundation of our enterprise is strengthening.

The Plymouth Rock Company's consolidated net income for 1994 was \$12.8 million, up from \$11.9 million the year before and representing a return on prior yearend equity of 23 percent. These numbers tell less of the story than one might wish. The impact of the fierce winter that besieged the Northeast is fully reflected in the net income. The bond market's damage, however, is not. New accounting rules applicable to our industry require losses suffered in the market value of bonds "available for sale" to go directly to the balance sheet without passing through the income statement. So, the published net income reflects only the realized portion of portfolio gains and losses. This year, unrealized losses predominated.

At the close of 1993, after an estimated provision for applicable taxes, there were \$2.6 million of unrealized capital gains in the consolidated bond portfolio. Under that year's rules, unrealized gains and losses were shown only in footnotes. One year later we sat with \$2.2 million in unrealized capital losses, which are now given their own line on the balance sheet. The net after-tax deterioration of \$4.8 million in our bond portfolio is what the income statement obscures. To restate last year's numbers on a comparable basis is inconsistent with the accounting rules, but it is straightforward to determine that the increase in our group's equity was little more than half the net income.

How large an enterprise is Plymouth Rock and how much of the total is other than Massachusetts automobile insurance? This is a pertinent question when the Company faces a cyclical turndown in its largest line of business, though size is not uniformly defined for insurers. Our group's total assets are \$250 million; we have about 330 employees; and our income statement shows revenues of \$117 million (measured after payment for reinsurance protection). None of these indices corresponds to my preferred measure of size, which is the gross revenue stream from our customers. That number does not appear on the income statement. Two useful approximations are the sum of published revenue and the cost of ceded reinsurance, as shown in the footnotes, and the total of incoming items, other than reinsured claims, on the cash flow statement. The first sum comes to \$158 million and would be higher by a few million if the published revenue were to be shown on a written basis; the second, on a cash basis, comes to \$162 million. An estimate of \$160 million is probably as reasonable a figure as needed of the Company's proprietary revenue stream.

So far, however, the estimate takes no account of the business under our management--but not our ownership--in New Jersey (about \$19 million in written premium) or the premium flows we service at Pilgrim Insurance Company for customers outside our own group (about \$10 million). If our size is appropriately defined by the stream of receipts implicated in either underwriting or management relationships, the total comes to nearly \$190 million. This statistic provides a useful index of both our workload and our profit potential over time. Since the Massachusetts private passenger automobile share of this grand total is about \$113 million, it might be fair to say that our receipts are 59 percent dependent on that single line and state combination. The fact that profits are more heavily weighted than revenues in the direction of Massachusetts auto is, I trust, a function of maturity. We have been in the auto insurance business now for eleven years, as opposed to just a few years for much of the rest.

Plymouth Rock Assurance Corporation is the Company's personal lines subsidiary responsible for the Massachusetts auto business and about \$18 million in Massachusetts homeowners premium. I think of it as the tree in our garden, and the other businesses as saplings. With a market share between three and four percent in Massachusetts, it has become the tenth largest personal lines writer here. Its 1994 was a bit too exciting for my taste, but in the end satisfactory. The adventure was in the homeowners arena, where the brunt of the winter storms was taken. In ordinary years, homeowners tends to run a lower pure loss ratio than the larger auto insurance line, and that is because it is so much worse in the bad years. This was one of those. The ultimate threat is an unprecedented hurricane season, but a winter of record snowfalls and recurring freezes is no blessing.

Plymouth Rock Assurance expected, based on budgeting for a normal New England winter, to pay out \$1.7 million in homeowners claims for the first quarter. It actually paid out two and a half times that, with most of the money going to cover damage from

ice dams on policyholders' roofs. More first quarter claims arrived belatedly as the year progressed. By yearend, the annual total of homeowners claims was still several million dollars above normal. Since net reinsurance costs in the homeowners line average several times those characterizing auto insurance, and all the usual commission and company expenses are at least as high, there is a thin margin for the payment of claims. This year's claims came to sixty-seven cents on the dollar, and the company lost money on homeowners coverage. Our overall loss ratio was spared by another successful year for auto insurance, an autumn season without a single hurricane, and a mild winter's start at yearend.

The expense ratio at Plymouth Rock Assurance continued its slow downward trajectory, improving almost half a point. Should we ever find Massachusetts transformed to a competitively rated state for auto insurance, every fraction of a point will make a potentially critical difference. Plymouth Rock Assurance treats it that way now. Having said that, I suspect we will have to give that company a year's grace in the long march next year. It is impossible to lower the overall expense ratio when the Insurance Commissioner has reduced rates and boosted agents commissions. The best one can hope for is a modest reduction in the company expense portion of the overall expense ratio, the total less commissions and premium taxes.

Plymouth Rock Assurance's goal for the foreseeable future is to maintain its moderate path of five to ten percent annual unit growth each year, while striving at all times to have the industry's best loss ratio and the market's best reputation for customer service. Let me stress that only the growth path is moderate; in our commitment to the two superlatives, moderation goes by the boards. A new executive, Alan Hines, has taken over the weighty responsibility for both the growth effort and the loss ratio. He joins Bill Kelley and Keith Rodney on the team primarily responsible for customer service.

The measurement of the growth objective in cars and houses rather than dollars accepts that, in years when the Commissioner raises the rates, premium growth will exceed unit growth. In years with rate decreases, the premium growth will lag the units. The coming year will see a rate decrease of about 6.1 percent, the first such cut in six years. The volume of business at Plymouth Rock Assurance, therefore, will be relatively flat throughout 1995. As other companies, especially those with dollar goals for annual growth, see how the new rates hurt their premiums, some may blindly bid for business just to meet quotas. That would make growth even more difficult in 1995. With our excellent reputation for service, we are well equipped to compete for the good business we are always seeking, but Plymouth Rock has no interest in meeting a top line goal at the expense of either quality or profits.

The Commissioner was probably not wrong to order a cut in rates. Premiums in the last few years have been ample, and the industry itself recommended a reduction for 1995.

Only the amount of the reduction was ever in question. If the Commissioner overshot the mark, as may have been the case, the industry will suffer a lean period. As I noted last year, though, the predominance of domestic companies places a practical limit on any potential inadequacy and its duration. There is simply no alternative to fair rates as a source of sufficient capital. I have always admired those who can make lemonade when life throws them lemons. The sudden shrinking of the premium stream is certainly a lemon, but a little lemonade is not beyond imagination. Markets that appear immune from cyclical correction are no good for rational competitors like Plymouth Rock Assurance. In the absence of a cycle, some folks can convince themselves that all business is forever profitable, and the starry-eyed fall over one another to acquire market share on uneconomic terms. We just saw a period like this come crashing to an end in real estate, and even more so in the real estate lending business. We prefer that bubbles are burst before they develop, and we accept the challenge ahead in Massachusetts personal lines with equanimity.

Last year, I reported that Peter Jones had reduced Mt Washington's 1992 losses by half and was hoping to reach breakeven in 1994. Despite the rough winter it appears that he accomplished exactly that, so I will uncork the bottle of champagne on ice for him. This is hardly a time to relax in Concord, however. Mt Washington is intended to be a clone of Plymouth Rock Assurance. It must someday match its larger sibling in both combined ratio and service reputation. The signs point in the right direction, but Mt Washington is struggling to achieve the necessary volume. The State of New Hampshire has less than one-sixth the personal lines premiums of Massachusetts. A drawn-to-scale copy of Plymouth Rock Assurance there would have about \$20 million in premium, which is probably about what a company in that environment needs to realize expense efficiencies. Mt Washington's premium volume, about \$7 million at last count, has not grown at all in the last twelve months. The task of getting the other \$13 million, in a market where companies and agents are more content than they are in Massachusetts or New Jersey, will fall to someone other than Peter. He signed on to get the company up and running, and will return to Massachusetts sometime in April.

The SRB group of companies had another year of quiet strengthening. While the four companies had a combined net income of only about half a million dollars, we hope this represents the tip of an iceberg with respect to their worth. Palisades Management Company, for example, is only a \$2 million company on our books, measured by revenues, and it lost \$160,000 last year. Yet, it is unquestionably the most valuable of the SRB companies. Its worth lies in the fact that it manages a much larger business, Palisades Safety and Insurance Association, which in turn is owned by its policyholders. When the insurer makes money, the management company will also prosper. That day may not be far off, and the potential scale of a New Jersey personal lines insurer is at least as great as that we have already built in Massachusetts.

Palisades, the insurer, is now writing \$19 million in premium, up from \$16 million at the end of the prior year. The news is actually better than that, though, because most of the progress occurred toward yearend and seems to represent a new momentum. After six months in which that business failed to grow, president Hal Belodoff lit a fire under the marketing effort and overhauled its staffing. The results have been rewarding. For the last quarter of 1994, Palisades business grew at a monthly rate of \$1 million in net new writings. This happens to be the same rate of growth averaged by Plymouth Rock Assurance over its eleven years. Hal believes he can maintain this rate in 1995, an essential prerequisite to cutting his expense ratio and reaching breakeven. While the quality of the business is looking good so far, the numbers are still a bit green for sophisticated analysis. I will have to save for next year a discussion of the all-important loss ratio.

Pilgrim Insurance, which provides services to other insurers and the residual market, had a good year. Vin Nieroda managed to add to both volume and profitability. I told him once that he would be considered a hero when he managed to earn a million dollars after taxes and did so within the context of an organization with which we would all be proud to be associated. He has taken that challenge to heart and swears that he will get us there within a few years. I would rather bet with that prediction than against it.

Boston Risk Management Corporation still operates at a small loss, but it has made progress nonetheless. BRMC now manages the workers compensation risks for a self-insured group of non-profit social service agencies. It has introduced an impressive program, called Comp 21, for intensive management of workers compensation costs more generally. I continue to believe that improved techniques of risk finance and loss management in workers compensation can save American business billions of dollars. While our entrance into that market has gone more slowly than contemplated, and the recent (almost certainly temporary) downward movement of traditional workers compensation premiums becalms for now the search for savings, there is no change in plans for BRMC. The opportunity is durable and the market is huge.

SRB Corporation itself is in the investment business, managing the portfolios of all the Plymouth Rock Companies. For the present, at least, it seeks no outside clients. The combined portfolios of the companies are now in excess of \$200 million, of which \$8.6 million is in common stocks and the remainder is held in fixed income instruments. The fixed income portfolio is conservatively invested, with an average credit quality of Aaa3 and an average duration of less than three years. Any unhedged portfolio of fixed income assets will be subject to a degree of interest rate risk. Although our exposure is far less than typical for the insurance industry, we saw the beast up close this year.

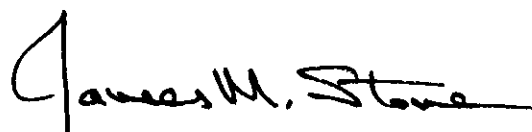
Avoidance of long-maturity instruments can be credited with having kept our total rate of return positive for the year. Negative total returns, I am told, abound for portfolio

managers and insurers in 1994. Wouldn't it be wonderful if we could have had a longer duration in the prior years, then shortened it or hedged it into a negative duration after the third quarter of last year? Yes, but that would have required a prognostication skill so powerful it would be wasted on mere financial enrichment. To one who believes no mortal is given that gift, our strategy still looks about right. We keep the bond portfolio quite conservative--but not radically so--and we take more risk for the prospect of greater returns on the equity side.

This posture is consistent with an underlying view that the interest rate market is relatively more efficient than the pricing of individual stocks and that free markets must invite equities to outperform bonds over long periods. It makes sense in such a world that whatever portion of an insurer's assets have to be protected from market fluctuation be invested without either equity risk or substantial interest rate risk. For us that means high quality, intermediate duration bonds. That part of the portfolio which can sustain market fluctuation is better directed toward equity positions than similarly risky long term debt, because the former are more susceptible to fundamental analysis and richer in the long run anyway. As we get larger, we will be placing an increasing share of our invested assets in selected equities.

Toward the close of 1994, we agreed to enter into a capital transaction which will give us two new shareholders and a new director. The amounts of money involved are not large, but the relationships are potentially important. Peter J. Wood is our new shareholder and director. He has built, in an astonishingly short period of time, the most successful personal lines insurer in the United Kingdom. Peter comes from a background in information technology and data processing. While our companies and their environments differ sharply, we look forward to having him question, challenge and compare the dichotomies. The other new shareholder will be an investment fund under the supervision of Morgan Stanley's merchant banking division. We already have a long-standing and productive relationship with Morgan Stanley, which this will only serve to deepen.

Next year may be the first in which Massachusetts personal auto insurance accounts for less than half of our managed, serviced and underwritten revenue stream. This will not be a minor event for Plymouth Rock. Making the best of increasing complexity and change requires good people: flexible, talented and prone to teamwork. I am aware of no insurer whose agency force, shareholders and staff are more amply endowed with these traits.

  
James M. Stone

## REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of  
The Plymouth Rock Company:

We have audited the accompanying consolidated balance sheets of The Plymouth Rock Company and subsidiaries as of December 31, 1994 and 1993, and the related consolidated statements of income, cash flows and changes in stockholders' equity for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Plymouth Rock Company and subsidiaries as of December 31, 1994 and 1993, and the consolidated results of their operations, and their cash flows for the years then ended, in conformity with generally accepted accounting principles.

As described in note 8 to the consolidated financial statements, in 1994 the Company changed its accounting for investment securities to conform to a newly promulgated financial accounting standard.

Boston, Massachusetts  
February 8, 1995

*Coopers & Lybrand* L.L.P.



**THE PLYMOUTH ROCK COMPANY**  
**CONSOLIDATED BALANCE SHEETS**

**December 31, 1994 and 1993**

<b>Assets</b>	<u>1994</u>	<u>1993</u>
Cash and marketable securities	\$187,230,410	\$163,869,322
Premiums receivable	9,300,333	7,499,583
Accrued investment income	2,283,082	2,216,764
Receivable from reinsurers	29,462,179	29,807,985
Deferred acquisition costs	8,088,075	6,999,376
Deferred income taxes	6,989,482	4,609,583
Fixed assets	4,975,457	5,983,763
Other assets	<u>1,826,369</u>	<u>532,006</u>
<b>Total assets</b>	<u><u>\$250,155,387</u></u>	<u><u>\$221,518,382</u></u>
<b>Liabilities</b>		
Claim and claim adjustment expense reserve	\$103,803,373	\$ 93,323,105
Premiums payable to reinsurers	25,146,939	28,100,289
Unearned premium reserve	27,113,845	23,142,077
Advance premium	9,857,880	10,517,615
Commissions payable and accrued liabilities	14,751,844	6,957,524
Unearned service fees	3,250,439	2,610,465
Other liabilities	<u>1,952,698</u>	<u>1,880,029</u>
<b>Total liabilities</b>	<u><u>185,877,018</u></u>	<u><u>166,531,104</u></u>
<b>Stockholders' Equity</b>		
Common stock and paid-in capital	10,536,024	10,536,024
Retained earnings	52,398,900	40,906,408
Net unrealized loss on investments	<u>(2,218,925)</u>	<u>-</u>
Common stockholders' equity	60,715,999	51,442,432
Minority interests in subsidiaries	<u>3,562,370</u>	<u>3,544,846</u>
<b>Total stockholders' equity, including minority interests</b>	<u><u>64,278,369</u></u>	<u><u>54,987,278</u></u>
<b>Total liabilities and stockholders' equity</b>	<u><u>\$250,155,387</u></u>	<u><u>\$221,518,382</u></u>

The accompanying notes are an integral  
part of the financial statements.

**THE PLYMOUTH ROCK COMPANY**  
**CONSOLIDATED STATEMENTS OF INCOME**  
For the years ended December 31, 1994 and 1993

<b>Revenues</b>	<u>1994</u>	<u>1993</u>
Premiums earned in underwriting activities	\$ 98,379,478	\$ 87,826,748
Fees earned from service activities	8,490,321	7,854,559
Investment income and capital gains	<u>10,154,394</u>	<u>11,566,252</u>
Total revenues	<u>117,024,193</u>	<u>107,247,559</u>
<b>Expenses</b>		
Claim and claim adjustment expenses	62,676,928	57,101,015
Policy acquisition, underwriting and general expenses	29,613,542	26,032,863
Service activity expenses	<u>7,950,566</u>	<u>7,485,163</u>
Total expenses	<u>100,241,036</u>	<u>90,619,041</u>
Income before federal income taxes	16,783,157	16,628,518
Federal income taxes	<u>3,964,262</u>	<u>4,696,276</u>
Net income	<u>\$ 12,818,895</u>	<u>\$ 11,932,242</u>

The accompanying notes are an integral  
part of the financial statements.

**THE PLYMOUTH ROCK COMPANY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

For the years ended December 31, 1994 and 1993

	<u>1994</u>	<u>1993</u>
<b>Cash flows from operating activities</b>		
Gross premiums collected	\$143,087,106	\$132,750,251
Reinsurance premiums paid	(44,939,518)	(37,913,360)
Finance charges collected	2,967,753	2,727,220
Fees and commissions collected	7,606,861	7,776,850
Investment income received	8,392,332	9,682,258
Gross claims and claim expenses paid	(85,078,426)	(71,784,985)
Reinsured claims and claim expenses collected	33,261,610	33,565,513
Policy acquisition, underwriting and general expenses paid	(30,592,016)	(27,285,403)
Federal income taxes paid	(5,306,422)	(7,582,201)
Service activity expenses paid	(8,266,043)	(4,983,806)
	<u>21,133,237</u>	<u>36,952,337</u>
<b>Cash flows from financing activities</b>		
Dividends to stockholders	(1,193,403)	(974,830)
Dividends to preferred stockholder of subsidiary	(140,000)	(140,000)
	<u>(1,333,403)</u>	<u>(1,114,830)</u>
Net cash used in financing activities	<u>(1,333,403)</u>	<u>(1,114,830)</u>
Net cash provided	<u>\$ 19,799,834</u>	<u>\$ 35,837,507</u>
<b>Investment of net cash provided</b>		
Net investment activity	\$ 18,723,661	\$ 34,099,805
Purchases of fixed assets	1,076,173	1,737,702
	<u>\$ 19,799,834</u>	<u>\$ 35,837,507</u>

The accompanying notes are an integral part of the financial statements.

## THE PLYMOUTH ROCK COMPANY

### CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the years ended December 31, 1994 and 1993

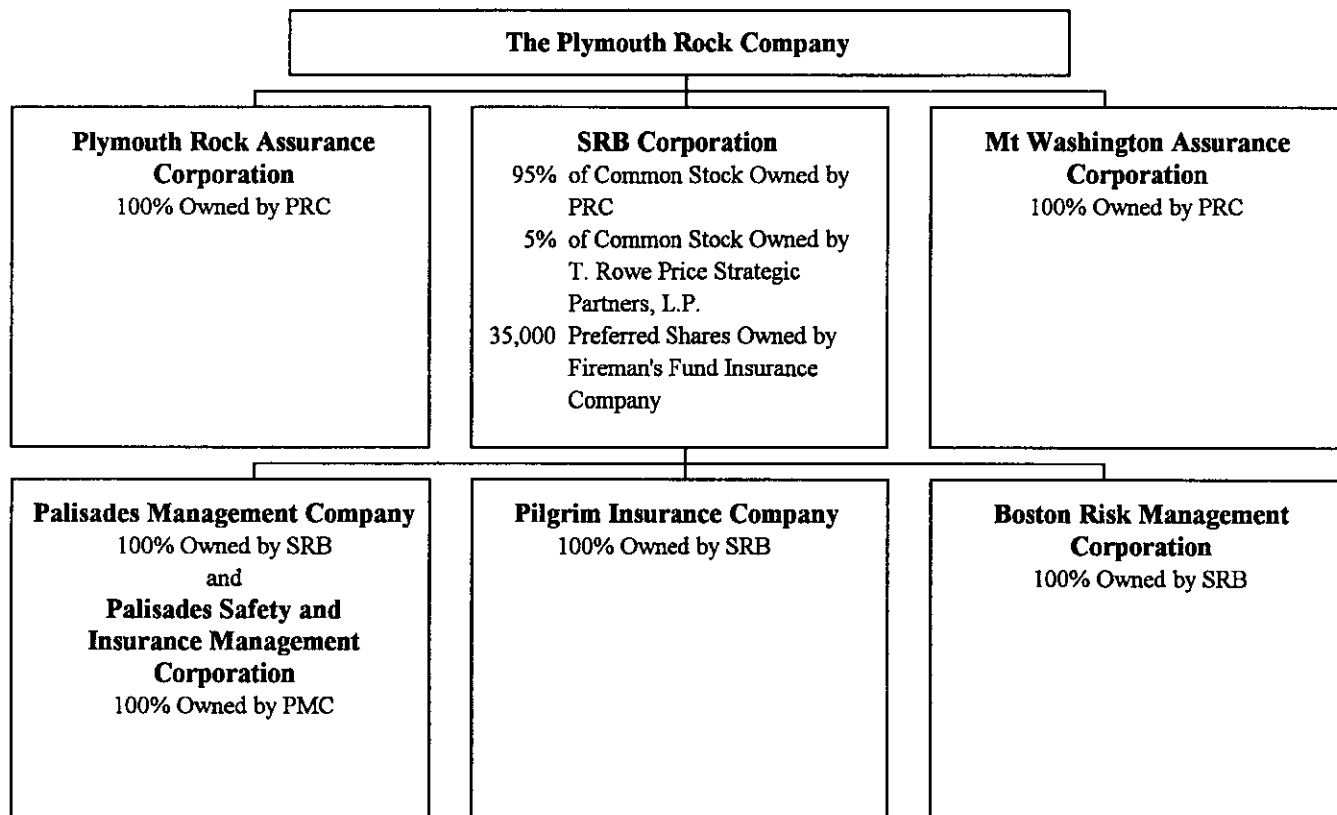
	<u>Common Stock and Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Net Unrealized Loss on Investments</u>	<u>Minority Interests</u>	<u>Total Stockholders' Equity</u>
December 31, 1992	\$10,536,024	\$30,081,996	\$ -	\$3,553,014	\$44,171,034
Net income	-0-	11,932,242	-	(1,168)	11,931,074
Dividends to stockholders	-0-	(974,830)	-	-0-	(974,830)
Dividends to preferred stockholder of subsidiary	<u>-0-</u>	<u>(133,000)</u>	<u>-</u>	<u>(7,000)</u>	<u>(140,000)</u>
December 31, 1993	10,536,024	40,906,408	-	3,544,846	54,987,278
Net unrealized gain at January 1, 1994	<u>-0-</u>	<u>-0-</u>	<u>2,586,086</u>	<u>-0-</u>	<u>2,586,086</u>
January 1, 1994	10,536,024	40,906,408	2,586,086	3,544,846	57,573,364
Net income	-0-	12,818,895	-0-	24,524	12,843,419
Dividends to stockholders	-0-	(1,193,403)	-0-	-0-	(1,193,403)
Dividends to preferred stockholder of subsidiary	-0-	(133,000)	-0-	(7,000)	(140,000)
Net unrealized loss during 1994	<u>-0-</u>	<u>-0-</u>	<u>(4,805,011)</u>	<u>-0-</u>	<u>(4,805,011)</u>
December 31, 1994	<u>\$10,536,024</u>	<u>\$52,398,900</u>	<u>\$(2,218,925)</u>	<u>\$3,562,370</u>	<u>\$64,278,369</u>

The accompanying notes are an integral  
part of the financial statements.

**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Organization of the Plymouth Rock Companies**

The corporate and ownership structure of the Plymouth Rock Companies is reflected in the following chart:



**2. Summary of Significant Accounting Policies**

**A. Principles of Consolidation**

The consolidated financial statements include the accounts of The Plymouth Rock Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform to 1994 reporting practices.

**B. Tangible Assets**

The cash and marketable securities category is composed primarily of fixed income investments, which are carried at market value in 1994 and amortized cost in 1993. The calculation of gain or loss on the sale of marketable securities is based on specific identification at the time of sale. The market values of investments are based on quoted market prices.

Fixed assets are carried at cost less accumulated depreciation. The Company provides for depreciation and amortization principally on the straight-line method over the estimated useful lives or the applicable lease terms.

# THE PLYMOUTH ROCK COMPANY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 2. Summary of Significant Accounting Policies, continued

#### C. Income Taxes

The Company files its federal income tax return on a consolidated basis. The Company's federal income tax return reflects current taxes which are not the same as the provision for income taxes shown in the Consolidated Statements of Income. This is because the rules of the Internal Revenue Code and those of generally accepted accounting principles can differ with respect to the time periods in which income and expenses are recognized.

Federal income taxes consist of:

	1994	1993
Current	\$5,201,078	\$5,996,998
Deferred	<u>(1,236,816)</u>	<u>(1,300,722)</u>
<b>Total</b>	<b><u>\$3,964,262</u></b>	<b><u>\$4,696,276</u></b>

Deferred income taxes in the balance sheet as of December 31, 1994 and 1993 consist of the net effect of these temporary differences:

	1994	1993
Discounting of claim reserves	\$3,276,058	\$2,733,704
Deferred income	2,559,000	2,312,002
Net unrealized loss on investments	1,143,083	-
Other	<u>11,341</u>	<u>(436,123)</u>
<b>Total</b>	<b><u>\$6,989,482</u></b>	<b><u>\$4,609,583</u></b>

The net unrealized loss on investments is presented in stockholders' equity, net of this estimate of applicable deferred income taxes.

The Company's reported provision for federal income taxes is less than that computed by applying the federal income tax rate for these years to income from operations before federal income taxes. This is principally because the Company receives significant non-taxable interest from state and municipal bonds.

#### D. Revenues Earned in Underwriting and Service Activities

Premium revenues are earned on a daily basis over the terms of the policies. Unearned premiums represent billed amounts which are applicable to the unexpired terms of policies in force and are presented net of reinsurance. Premiums receivable are net of reserves for doubtful collections of \$382,006 and \$395,006 at December 31, 1994 and 1993, respectively, and are presented net of unbilled amounts of \$14,508,952 and \$14,848,362, respectively.

The Company derives fee income by providing insurance, investment management, brokerage, policy processing, billing, claims management and systems development services. Fee income is earned over the related contract periods.

**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**2. Summary of Significant Accounting Policies, continued**

**E. Reinsurance**

Treaty reinsurance is used to reduce exposure to large claims. The Company regularly evaluates the financial condition of its reinsurer and monitors the concentration of credit risk to minimize significant exposure. The Company maintains catastrophe, quota share and excess of loss contracts that are prospective in nature and remains primarily liable as the direct insurer on all voluntary risks.

Amounts recoverable for claim reserves and paid claims are reflected as receivable from reinsurers. The income statement is reflected net of reinsurance activity as follows:

	1994		1993	
	Premiums Written	Losses Incurred	Premiums Written	Losses Incurred
Gross Ceded	\$142,073,842 (40,037,561)	\$95,592,732 (32,915,804)	\$137,158,889 (44,238,389)	\$85,393,287 (28,292,272)
Net	<u>\$102,036,281</u>	<u>\$62,676,928</u>	<u>\$ 92,920,500</u>	<u>\$57,101,015</u>

Ceded premiums earned for 1994 and 1993 were \$41,134,866 and \$42,385,485 respectively.

The Company has a 40 percent quota share reinsurance treaty which reinsures certain coverages for losses in excess of approximately 88 percent of premiums earned during specified accounting periods. Revenues and expenses are reflected net of quota reinsurance totaling approximately \$23 million and \$20 million for 1994 and 1993, respectively.

The Company has a catastrophe reinsurance treaty. At December 31, 1994, the Company had paid approximately \$1,750,000 (net of cumulative losses and commissions) to the reinsurer to cover future catastrophes. The contract has an experience rating feature whereby a substantial portion of the amount paid could be returned to the Company if the experience continues to be favorable.

The Company is a member of Commonwealth Automobile Reinsurers and accounts for ceded policies as reinsurance. The Company's estimated share of the Commonwealth Automobile Reinsurers deficit is recorded in claim and claim adjustment expenses.

The Company acts as an intermediary for certain other insurance companies in administering commercial automobile insurance programs. The Company's income statement and reinsurance activity exclude premiums earned of \$13,402,145 and \$11,970,158 and claim and claim adjustment expenses of \$5,453,459 and \$4,643,130 in 1994 and 1993, respectively. In connection with these arrangements, receivables and claim reserves exclude \$3,068,445 and \$3,816,242 at December 31, 1994 and 1993, respectively.

**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**2. Summary of Significant Accounting Policies, continued**

**F. Deferred Acquisition Costs**

Commissions and premium taxes are deferred and amortized pro rata over the contract periods in which the related premiums are earned. All amounts deferred at December 31 are charged to operations in the following year as the related premiums are earned. Deferred acquisition costs are presented net of deferred commission income on ceded reinsurance.

**G. Claim and Claim Adjustment Expenses**

Claim reserves represent the estimated liability for claims reported to the Company plus reserves for claims incurred but not yet reported. Claim adjustment expense reserves represent the estimated expenses related to settling these claims. Claim and claim adjustment expense reserves are presented before estimated recovery for reinsurance. The methods of making such estimates and establishing the resulting reserves are reviewed regularly, and any adjustments are reflected in income currently. Losses incurred in 1994 and 1993 include payments for events reported in prior years. Payments for prior reported events amounted to approximately \$35.9 million and \$28.6 million in 1994 and 1993, respectively. Reserves carried for these claims at prior year end were \$42.1 million and \$33.8 million, respectively. Claim and claim adjustment expense reserves at December 31, 1992 were approximately \$79.7 million.

**3. Consolidated Revenues**

Revenues, net of reinsurance, for the separate companies for 1994 and 1993 are:

	1994	1993
The Plymouth Rock Company	\$ 3,260,436	\$ 2,588,642
Plymouth Rock Assurance Corporation	104,216,892	93,914,493
Mt Washington Assurance Corporation	3,321,346	4,449,752
SRB Corporation	5,761,724	6,109,776
Pilgrim Insurance Company	5,778,122	5,092,471
Palisades Management Company (Consolidated)	1,910,330	1,940,959
Boston Risk Management Corporation	346,640	329,490
	124,595,490	114,425,583
Intercompany eliminations	(7,571,297)	(7,178,024)
Total revenues	\$117,024,193	\$107,247,559

**4. Savings and Investment Plan and Deferred Compensation Plan**

The Company has a Savings and Investment Plan under Section 401(k) of the Internal Revenue Code. The Plan, which is a defined contribution plan, covers all employees 21 years or older with at least one year of service. The Company provided \$660,229 and \$574,164 for discretionary contributions in 1994 and 1993, respectively.



**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**4. Savings and Investment Plan and Deferred Compensation Plan, continued**

The Company has a Deferred Compensation Plan for officers, managers and directors other than its founding shareholders. The Plan provides for a rate of return on voluntary deferrals based on the financial performance of the Company. The Company has accrued \$743,228 and \$261,246 as of December 31, 1994 and 1993, respectively for liabilities relating to the Plan.

**5. Reconciliation of Net Income to Net Cash Provided by Operating Activities**

The following noncash charges to income account for the differences between net income and net cash provided by operating activities:

	<u>1994</u>	<u>1993</u>
Net income	\$12,818,895	\$11,932,242
Depreciation and amortization	2,394,525	2,170,914
Minority interests	24,524	(1,168)
Change in premiums receivable	(1,800,750)	(675,186)
Change in accrued investment income	(66,318)	(385,192)
Change in receivable from reinsurers	345,806	5,273,241
Change in deferred acquisition costs	(1,088,699)	(1,294,133)
Change in deferred income taxes	(1,236,816)	(1,300,722)
Change in claim and claim adjustment expense reserve	10,480,268	13,629,722
Change in premiums payable to reinsurers	(2,953,350)	3,574,914
Change in unearned premium reserve	3,971,768	2,786,926
Change in advance premium	(659,735)	684,615
Change in commissions payable and accrued liabilities	(205,115)	1,249,534
Change in unearned service fees	639,974	838,435
Change in other assets and other liabilities	(2,198,076)	355,480
Income on sale of investment securities	673,313	(1,856,853)
Income on disposal of fixed assets	(6,977)	(30,432)
Net cash provided by operating activities	<u>\$21,133,237</u>	<u>\$36,952,337</u>

**6. Fixed Assets**

The table below summarizes fixed assets at December 31, 1994 and 1993. Purchases of fixed assets were \$1,076,173 and \$1,737,702 in 1994 and 1993, respectively.

	<u>Useful Lives</u>	<u>1994</u>	<u>1993</u>
Furniture and fixtures	5-10 years	\$ 2,852,622	\$ 3,449,168
Computers	3-5 years	4,830,664	5,670,416
Leasehold improvements	2-6 years	2,343,533	2,325,661
Vehicles	3 years	<u>650,777</u>	<u>608,844</u>
Total cost		10,677,596	12,054,089
Less: accumulated depreciation and amortization		<u>5,702,139</u>	<u>6,070,326</u>
Net book value		<u>\$ 4,975,457</u>	<u>\$ 5,983,763</u>

## THE PLYMOUTH ROCK COMPANY

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 7. Lease Commitments

Rental expenses for 1994 and 1993 aggregated approximately \$1,663,000 and \$1,598,000, respectively. There are several leases totaling approximately 81,000 square feet of office space and 22,500 square feet of storage space. Certain leases contain renewal options which may be exercised from three to twelve months prior to expiration. For each of the years 1995 through 2000, the minimum lease obligations of the Company are approximately \$1,053,000 annually. The total obligation for leases through 2000 is approximately \$6,319,000.

#### 8. Investments and Investment Income

Effective January 1, 1994, the Company changed its accounting for investment securities to conform to a newly promulgated financial accounting standard. All securities presently held are classified as Available for Sale and are now carried at market value. Net unrealized capital gains and losses on Available for Sale securities, net of applicable deferred taxes, are credited or charged directly to stockholders' equity.

##### A. Composition of Investment Portfolio

At December 31, 1994 and 1993, amortized cost, unrealized gains and losses before federal income taxes and market value of cash and marketable securities are as follows:

At December 31, 1994:	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
Cash and cash equivalents	\$ 30,032,476	\$ -0-	\$ 2,625	\$ 30,029,851
U.S. government securities	13,547,694	234	543,542	13,004,386
State and municipal securities	97,318,958	224,102	2,538,210	95,004,850
Corporate debt securities	31,831,478	56,916	985,212	30,903,182
Mortgage-backed securities	9,997,454	-0-	275,976	9,721,478
Common stocks	7,864,358	733,730	31,425	8,566,663
<b>Total</b>	<b>\$190,592,418</b>	<b>\$1,014,982</b>	<b>\$4,376,990</b>	<b>\$187,230,410</b>

At December 31, 1993:	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
Cash and cash equivalents	\$ 13,774,325	\$ -0-	\$ -0-	\$ 13,774,325
U.S. government securities	11,239,960	17,936	55,316	11,202,580
State and municipal securities	97,824,572	2,919,470	22,788	100,721,254
Corporate debt securities	28,731,301	850,998	74,516	29,507,783
Mortgage-backed securities	9,000,847	61,758	19,464	9,043,141
Common stocks	3,298,317	240,234	-0-	3,538,551
<b>Total</b>	<b>\$163,869,322</b>	<b>\$4,090,396</b>	<b>\$ 172,084</b>	<b>\$167,787,634</b>

**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**8. Investments and Investment Income, continued**

**A. Composition of Investment Portfolio, continued**

At December 31, 1994, maturities of cash and marketable securities are as follows:

	<u>Amortized Cost</u>	<u>Market Value</u>
Cash	\$ 23,527,482	\$ 23,527,482
Due in 90 days or less	6,504,994	6,502,369
Due after 90 days and in one year or less	16,775,950	16,655,887
Due after one year and in five years or less	107,982,662	104,715,739
Due after five years	27,936,972	27,262,270
Common stocks	7,864,358	8,566,663
Total	<u>\$190,592,418</u>	<u>\$187,230,410</u>

**B. Investment Activity**

The components of investment activity during 1994 and 1993 are as follows:

	<u>1994</u>	<u>1993</u>
Balance at beginning of year	\$163,869,322	\$129,769,517
Change in marketable securities:		
Sales prior to maturity	(70,886,677)	(93,467,185)
Redemptions at maturity	(3,150,040)	(1,549,838)
Purchases	76,502,227	124,415,844
Change in marketable securities	2,465,510	29,398,821
Change in cash and cash equivalents	16,258,151	4,700,984
Net investment activity	18,723,661	34,099,805
Purchases in process	7,999,435	-0-
Net unrealized loss on investments	(3,362,008)	-
Balance at end of year	<u>\$187,230,410</u>	<u>\$163,869,322</u>

**C. Analysis of Investment Income and Capital Gains**

The components of investment income and capital gains before federal taxes during 1994 and 1993 are as follows:

	<u>1994</u>	<u>1993</u>
Interest income from securities	\$ 8,818,706	\$ 7,933,327
Finance charges from premiums receivable	2,967,753	2,727,220
Gross investment income	11,786,459	10,660,547
Investment expenses	(958,752)	(951,148)
Investment income	10,827,707	9,709,399
Realized capital gains	(673,313)	1,856,853
Investment income and capital gains	<u>\$10,154,394</u>	<u>\$11,566,252</u>

**THE PLYMOUTH ROCK COMPANY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**9. Stockholders' Equity**

**A. Common Stock**

Common stock at December 31, 1994 and 1993 is composed of Class A common and Class B common shares, both classes having a par value of \$.10 per share. There are 300,000 Class A shares authorized, of which 130,905 and 130,572 were issued and outstanding on December 31, 1994 and 1993, respectively. There are 90,000 Class B shares authorized, of which 87,667 and 88,000 were issued and outstanding on December 31, 1994 and 1993, respectively.

The Class A common shares are fully transferable and have the right to elect 20 percent of the Board of Directors. The Class B common shares are not transferable, but may be converted to Class A common shares on a one for one basis at any time at the option of the holder, or automatically upon the occurrence of certain events. The Class B common shares elect 80 percent of the Board of Directors.

**B. Preferred Stockholder's Interest in Subsidiary**

A subsidiary of the Company has issued 35,000 shares of cumulative preferred stock with no par value, all of which were outstanding at December 31, 1994 and 1993. The preferred stockholder is entitled to receive cumulative cash dividends of 4 percent per year, increasing to 7 percent per year under certain circumstances, when declared by the subsidiary's Board of Directors out of funds legally available. The preferred stockholder is also entitled to receive special cumulative dividends of 20 percent of the difference between the subsidiary's net income and the amount of regular preferred dividends for that year. Such special dividends are limited to \$1,000,000 on a cumulative basis. Under certain conditions the preferred shares may be redeemed by the subsidiary at \$120 per share with adjustment for dividends. In addition, under certain circumstances the holder may redeem the preferred stock at \$100 per share plus any accrued but unpaid dividends. In the event of corporate liquidation, the preferred stockholder of the subsidiary is entitled to receive out of available subsidiary funds \$120 per share (\$4,200,000 in the aggregate), with adjustment for certain dividends paid, plus any accrued but unpaid dividends. The preferred stock is convertible under certain default circumstances, with appropriate regulatory approval, into specified amounts of the subsidiary's common stock.

**C. Statutory Surplus and Dividend Availability**

The Company's insurance subsidiaries are required to file financial statements with state insurance departments. The accounting principles prescribed or permitted for these financial statements differ in certain respects from generally accepted accounting principles. On a statutory accounting basis, capital and surplus of the Company's insurance subsidiaries aggregated approximately \$45,698,000 and \$39,923,000 at December 31, 1994 and 1993, respectively. Regulatory limits restrict the amount of dividends which can be remitted to the Company from its insurance subsidiaries without approval of state insurance regulators.

## Directors and Officers of The Plymouth Rock Company

### Directors

James M. Stone, *Chairman*

James N. Bailey

Michael J. Johnston

Wilmot H. Kidd, III

Keith R. Rodney

Benno C. Schmidt

Peter J. Wood

### Officers

James M. Stone  
*President*

Keith R. Rodney  
*Executive Vice President and Clerk*

James N. Bailey  
*Treasurer*

William M. Kelley  
*Vice President*

## Directors and Officers of the Plymouth Rock Group of Companies

### Non-Management Directors

Normand A. Dion  
Alexander Ellis, III  
Michael J. Johnston  
Wilmot H. Kidd, III  
John F. Meyer  
Eugene J. Meyung  
Benno C. Schmidt  
David L. Warnock  
Peter J. Wood

### Management Officers and Directors

Francis P. Arment  
James N. Bailey  
Hal Belodoff  
Elyse D. Cherry  
Frederic C. Church, Jr.  
Paula W. Gold  
Alan M. Hines  
Peter R. Jones  
J. Robert Keiger  
William M. Kelley  
Stewart W. Kemp  
Raymond D. Moore  
Vincent V. Nieroda  
Keith R. Rodney  
James M. Stone

Independent Accountants:  
Coopers & Lybrand L.L.P.

Counsel:  
Ropes & Gray